National Energy Board | Office national de l'énergie

Reasons for Decision

TransCanada PipeLines Limited

RH-001-2014

December 2014

Part IV Tolls and Tariff

Canada

National Energy Board

Reasons for Decision

In the Matter of

TransCanada PipeLines Limited

2015 – 2030 Tolls and Tariff Application

RH-001-2014

December 2014

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Glossary of Terms and Abbreviations

ABA	Annual bridging amount
AECO	The Alberta gas trading price and is one of North America's leading price-setting benchmarks
BAA	Bridging amortization account
Basis Point	One-hundredth of a percentage point; used in reference to interest rates or rates of return
Bcf	Billion cubic feet
Bps	Basis points
Bridging Contribution	A contribution to the costs of the Western Mainline not otherwise recovered through the Compliance Tolls
Business risk	The risk attributed to the nature of a particular business activity (as distinct from financial risk); for pipelines, it typically includes supply, market, regulatory, competitive, and operating risk
Capital structure	The way in which a business is financed; generally expressed as a percentage breakdown of the types of capital employed
CDA	Central delivery area
Competitive risk	The business risk that results from competition for customers at both the supply and market ends of a pipeline system
Compliance Tolls	Tolls resulting from the RH-003-2011 hearing and decision
DDA	Distributor delivery area
Deemed debt ratio	The percentage of an entity's total capital structure financed by debt; as approved by the regulator for tolling purposes
Deemed equity ratio	The percentage of an entity's total capital structure financed by equity; as approved by the regulator for tolling purposes
DMR	Discretionary miscellaneous revenue
ECDA	East central delivery area

EDA	Eastern delivery area
ELTRO	Early long-term renewal option
Embedded cost of debt	The weighted-average historical cost of debt outstanding
Financial risk	The risk inherent by utilizing debt in a company's capital structure; financial risk increases as the proportion of debt increases
FT	firm transportation
GJ	Gigajoule
GLGT	Great Lakes Gas Transmission Company
ICE	Intercontinental Exchange – A network of regulated exchanges and clearinghouses for financial and commodity markets, including natural gas
IT	Interruptible transportation
LTAA	Long-term adjustment account
Market risk	The business risk that stems from the overall size of the market share that a pipeline is able to capture
MDA	Manitoba delivery area
NGX	Canadian Natural Gas Index – A recognized exchange and clearing agency in Alberta that brings efficiency pricing transparency to the natural gas and electricity markets. It is also a registered derivatives clearing house
NIT	NOVA Inventory Transfer – NIT is a Western Canada Sedimentary Basin gas-trading hub for customers on the Nova Gas Transmission Limited system
NOL	Northern Ontario Line – a segment of the Mainline
OM&A	Operations maintenance and administration
PJ	Petajoule
PG&E Gate	A virtual trading point on the California Gas Transmission system

RAM	Risk alleviation mechanism
Regulatory risk	Risk to the income-earning capability of the assets that arises due to the method of regulation of the company
ROE	Return on equity
Settlement	The settlement agreement negotiated between TransCanada, Enbridge Gas Distribution Inc., Société en commandite Gaz Métro and Union Gas Limited that forms the basis for the application at issue in this proceeding
STFT	Short term firm transportation
Supply risk	The risk that the physical availability of natural gas could affect a pipeline's income-earning ability
SWDA	Southwestern delivery area
TBO	Transportation by others
TJ/day	Terajoules per day
TQM	Trans Québec and Maritimes Pipeline Inc.
TransCanada Contribution	A $20 million after-tax contribution by TransCanada to the Mainline revenue requirement from 2015 to 2020
UDC	Unutilized demand charge
Variability risk	The risk resulting from factors that affect year-to-year earnings and cash flow for the pipeline
WCSB	Western Canada Sedimentary Basin
Western Mainline	Two segments of the Mainline, the Prairies Line and the Northern Ontario Line, are collectively referred to as the Western Mainline

Recital and Appearances

IN THE MATTER OF the *National Energy Board Act* and the Regulations made thereunder;

IN THE MATTER OF an application dated 20 December 2013 by TransCanada PipeLines Limited (TransCanada) under Part IV of the *National Energy Board Act* for orders approving, among other things, tolls that TransCanada may charge for transportation services provided on its Mainline pipeline system (Mainline) between 1 January 2015 and 31 December 2020 under file OF-Tolls-Group1-T211-2013-05 01; and

IN THE MATTER OF Hearing Order RH-001-2014 dated 9 May 2014.

HEARD in Calgary, Alberta on 9, 10, 11, 12, 15, 16, 17, 18, 19, 23, 24 and 25 September 2014;

BEFORE:

R. R. George	Presiding Member
R. R. Wallace	Member
J. Gauthier	Member

Appearances	**Participants**	**Witnesses**
C. K. Yates, Q.C. R. Hofley M. C. Davis	TransCanada PipeLines Limited	K. Johannson N. Bowman D. Schultz K. Hirak J. J. Reed P. R. Carpenter
D. A. Holgate A. Sears	Alberta NorthEast Gas, Limited	J. Carmichael J. P. Rudiak J. A. Stanzione D. P. Yardley
L. Jamieson J. H. Smellie R. M. Vandergrift	BP Canada Energy Group ULC	
L. Manning	Canadian Association of Petroleum Producers	S. Mueller R. Cusson D. Thorn R. Orans R. Mikkelsen

H. Van Iderstine B. Czarnecki	Centra Gas Manitoba, Inc.	L. Stewart N. Kostick B. Sanderson C. Cicchetti
D. Dufour	Dufour Energy Commodities	
R. Fischer L. E. Smith	Enbridge Gas Distribution Inc.	M. Giridhar R. Fleck J. Makholm
R. Powell	Encana Corporation	
C. King	Alberta Department of Energy	
R. Twyman	Industrial Gas Users Association	
J.-F. Lord	Ministére de l'Énergie et des Ressources naturelles du Québec	
I. Mondrow	Northland Power Inc.	
L. E. DeMarco D. Kloeze	Ontario Ministry of Energy	
E. Dunberry M.-C. Hivon P. Cabana D. Rhéaume	Société en commandite Gaz Métro	P. Cabana R. Fleck J. Makholm
L. Fitzpatrick	Suncor Energy Marketing	
G. Giesbrecht	Talisman Energy Inc.	
T. Lange	Tenaska Marketing Canada, Division of DMV Corp.	
L. E. Smith	Union Gas Limited	M. Isherwood R. Fleck J. Makholm
L. Sherret A. Hudson	National Energy Board	

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Disposition

The Letter Decision issued on 28 November 2014 and the following chapters constitute our Decision and Reasons for Decision in respect of TransCanada's Application heard by the Board in the RH-001-2014 proceeding.

LETTER DECISION

File OF-Tolls-Group1-T211-2013-05 01
28 November 2014

To: All parties to RH-001-2014

TransCanada PipeLines Limited (TransCanada)
Application for Approval of 2015 to 2030 Tolls (application)
RH-001-2014 Decision with Reasons to Follow

On 20 December 2013, TransCanada filed an application for approval of a settlement agreement (Settlement) for its Mainline System (Mainline). The existing tolls and tariff for the TransCanada Mainline were determined by the RH-003-2011 Decision rendered in March 2013. The present application was filed pursuant to Parts I and IV of the *National Energy Board Act*, the 2002 *National Energy Board Guidelines for Negotiated Settlements of Traffic, Tolls and Tariffs* (Settlement Guidelines) and certain directives in the RH-003-2011 Decision. Specifically the application asked the National Energy Board (NEB or Board) to:

- approve the negotiated settlement;
- set Mainline tolls in accordance with the Second Amended Appendix D to the settlement for services for 2015 to 2020 and for approval of a methodology for setting tolls to 2030;
- revise the tariff in accordance with Attachment 3 to the application; and
- grant such further and other relief as TransCanada may request or the Board may consider appropriate.

The Settlement was reached between TransCanada and the three largest Mainline customers and largest Canadian local distribution companies – Enbridge Gas Distribution Inc., Union Gas Limited and Gaz Métro Limited Partnership.

Following receipt of the application, the Board initiated a comment process among TransCanada shippers and stakeholders. At the conclusion of the comment process, the Board found that it could not approve the Settlement as a contested settlement under the Board's Settlement Guidelines.

The Board indicated its willingness to treat the Settlement as a common position of the parties to it in a contested tolls application, which TransCanada agreed to on 14 April 2014.

The Board issued a Hearing Order on 9 May 2014, setting the application down for an oral public hearing. The oral portion of the hearing took place in Calgary over 12 days in September 2014.

There were 33 intervenors and 4 commenters that were granted standing in the process.

The Board has decided to release its decision on the application with reasons to follow. It is the Board's view that there is a benefit to the market by having a timely decision. Reasons for the decision will be released on or before 18 December 2014. The Board's decisions on the components of the application follow.

Need for the application

The Board recognizes that off-ramps were included in the RH-003-2011 Decision to account for material changes affecting the Mainline. In the Board's view, such a material change in the financial position of the Mainline, as well as in its market circumstances since the implementation of the RH-003-2011 tolls, have occurred.

The Board has considered the relevant evidence placed on the record, including the contractual commitments made by the settling parties, in reaching its decision that the resulting tolls are just and reasonable and not unjustly discriminatory.

New services

The Board approves the following service amendments that TransCanada proposed:

- the 15-year minimum contract term requirement for expansion facilities;
- the introduction of an option and process for shippers to convert their long-haul firm transportation contracts to short-haul firm service contracts;
- minor amendments to diversion and alternate receipt point rights;
- modifications to certain distributor delivery areas and the establishment of new delivery locations;
- the new summer storage service; and
- the new enhanced market balancing service.

Renewal provisions

The Board approves TransCanada's proposed term-up provision. The term-up provision will come into effect on 30 March 2015.

Pricing discretion

The Board approves maintaining pricing discretion as established in the RH-003-2011 Decision. As discussed in Toll Design below, the Board will review the continued appropriateness of the existing pricing discretion for the 2018 to 2020 time period in a future TransCanada Mainline tolls application.

During the oral hearing, TransCanada submitted that its pricing desk employees have access to non-public information, including path-specific shippers' nominations. The Board is concerned that access to non-public information available to TransCanada's pricing desk employees could be construed to offer an unfair advantage to TransCanada over secondary market participants.

The Board directs TransCanada to initiate a comprehensive review of the non-public, shipper-specific information that TransCanada's pricing desk has access to, including non-public information on TransCanada's affiliates, and how this non-public information could, in theory and practice, influence the setting of bid floors for interruptible transportation and short-term firm transportation. The Board is primarily concerned about access of pricing desk employees to shippers' transactions, including volumes and transportation paths, real time and historic.

TransCanada is directed to provide remedies on how it will prevent access to and use of non-public information in the setting of bid floors for discretionary services. Potential remedies may include the implementation of firewalls between the pricing desk and the regulated Mainline entity, inclusive of communications and access to information; a separate code of ethics for pricing desk employees; and/or an update to the Mainline's Code of Conduct, amongst others. Given the concerns expressed by participants in this proceeding, the Board is of the view that TransCanada's review will benefit from consulting with Mainline stakeholders on this matter. TransCanada is directed to provide the results of its internal review and consultations with stakeholders to the Board by 31 March 2015.

TransCanada is already under the direction of the Board to consult with shippers on the content of its Quarterly Surveillance Reports and whether any amendments need to be made to reporting requirements. This is a direction which flows from the Board's response to TransCanada's Compliance Filing under RH-003-2011 in June 2013 and for which TransCanada was recently granted a time extension. The Board in this proceeding directs TransCanada to review and consult on its internal management of non-public information as it relates to its exercise of pricing discretion. The Board anticipates that TransCanada will take advantage of the connections between these issues and the consultation on reporting requirements and engage its stakeholders on both.

In addition to participating in the aforementioned consultations, the Board further invites interested parties to review TransCanada's 31 March 2015 submission and provide their comments to the Board by 30 April 2015. Upon receipt of submissions from interested parties, the Board may hold a written process or a technical conference to determine measures to address the transparency and management of discretionary services issues.

Revenue requirement and rate base

The Board approves the proposed revenue requirements for 2015 to 2020, including the return and income tax, TransCanada Contribution, Bridging Contribution and other cost of service elements.

The Board approves the proposed rate base components for 2015 to 2020, including the adjustment accounts – the Long-Term Adjustment Account (LTAA) and the Bridging Amortization Account – and the Capacity Capital Additions allocated to the Eastern Triangle rate base.

The Board approves the proposed treatment of the LTAA as an adjustment account to eliminate any and all variances between the actual and forecast revenue requirement and the actual and forecast revenue during the period 1 January 2015 to 31 December 2020, net of incentive mechanism adjustments.

The Board approves the allocation of the actual Toll Stabilization Account (TSA) balance as of 31 December 2014 to the LTAA and the subsequent elimination of the TSA.

The Board notes that TransCanada proposes to allocate the LTAA balance to the Eastern Triangle rate base in 2021. The Board determines that this proposal is appropriate in the context of the package of gives-and-takes between TransCanada and the settling parties. However, based on the circumstances when 2021 tolls are determined, the Board may determine that a different allocation of the LTAA is more appropriate.

The Board approves the recovery of the Bridging Contribution attributable to the Eastern Triangle tolls over the period 1 January 2015 to 31 December 2030 as applied for.

The Board notes that the segmentation tolling parameter relates to a future period. The Board approves the segmentation tolling parameter in principle at this time. The Board will continue to monitor the appropriateness of the segmentation tolling parameter prior to its implementation. Should the circumstances be significantly different closer to 2020, the Board would expect that the issue of segmentation post-2020 would be re-examined to determine if it remains appropriate.

Toll design

The Board approves TransCanada's proposed three step toll design for 2015 to 2020 subject to the requirement that TransCanada file the following two documents:

1) RH-001-2014 compliance filing – This is to be filed before 31 March 2015 and must include the following adjustments to the proposed tolls: the allocation of the actual TSA balance as of 31 December 2014 to the LTAA and, all updates to revenue requirement and firm billing determinants as of 31 December 2014.

   The requirement for a compliance filing necessitates interim tolls. Therefore, the applied-for tolls are to be implemented on an interim basis on 1 January 2015. Differences recorded due to charging the interim toll from 1 January 2015 until the date of the compliance filing are to be captured in the LTAA.

2) 2018 to 2020 toll application - This application is to be filed prior to 31 December 2017 and must include the following:

- A review of revenue requirements, including return, income taxes, the annual bridging amount and the LTAA balance, for the 2018 to 2020 period;
- A review of billing determinants, including long-haul contracted quantities to the Eastern Triangle;
- A review of discretionary miscellaneous revenue forecasts for the 2018 to 2020 period; and
- A discussion of any other material changes that would impact the operation of the Mainline for the 2018 to 2020 period.

At that time, the Board may consider whether pricing discretion continues to be necessary, either on an integrated or a segmented basis. The Board expects TransCanada to file the 2018 to 2020 toll application for approval regardless of whether the application is expected to result in a toll change for the 2018 to 2020 period.

The Board approves rolled-in tolling into the Eastern Triangle rate base of the Eastern Triangle capital expansions between 2015 and 2020, and approves in principle the practice of rolling-in Mainline facilities costs in the future regime after segmentation such that the costs of facility additions in the Eastern Triangle will be reflected in Eastern Triangle tolls until 2030. The Board notes, however, that each facilities application is unique, and the reasonableness of continuing the practice of rolled-in tolling will be considered by the Board in its assessment of each application.

The Board also approves the applied-for firm service billing determinants, subject to the updates stated above, and discretionary miscellaneous revenue forecasts. In the Board's view, the implementation of the proposed toll design will result in just and reasonable tolls.

Risks and rewards

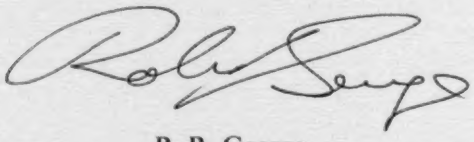
The Board finds that the 10.1 per cent return on equity and 40 per cent deemed equity ratio is a fair return for the Mainline, commensurate with its risk under the proposal, and in accordance with the fair return standard.

The Board approves the cost of debt as proposed by TransCanada and 60 per cent deemed debt ratio.

The Board approves the applied-for incentive sharing mechanism.

Disposition

The foregoing constitutes our Decision in respect of TransCanada's Application for Approval of 2015 to 2030 Tolls heard by the Board in the RH-001-2014 proceeding.



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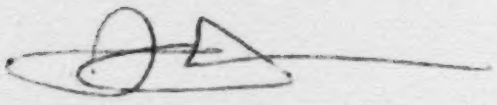
Presiding Member



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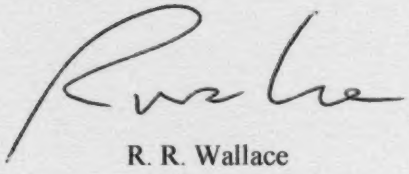
Member



R. R. Wallace
Member

Calgary, Alberta
November 2014

Chapter 1

Introduction and Background

1.1 Overview of the application and hearing

On 20 December 2013, TransCanada filed an application for approval of a settlement agreement (Settlement) for its Mainline System (Mainline). The existing tolls and tariff for the TransCanada Mainline were determined by the RH-003-2011 Decision rendered in March 2013. The present application was filed pursuant to Parts I and IV of the *National Energy Board Act*, the 2002 *National Energy Board Guidelines for Negotiated Settlements of Traffic, Tolls and Tariffs* (Settlement Guidelines) and certain directives in the RH-003-2011 Decision. Specifically the application asked the Board to:

- approve the negotiated settlement;
- set Mainline tolls in accordance with the Second Amended Appendix D to the settlement for services for 2015 to 2020 and for approval of a methodology for setting tolls to 2030;
- revise the tariff in accordance with Attachment 3 to the application; and
- grant such further and other relief as TransCanada may request or the Board may consider appropriate.

The Settlement was reached between TransCanada and the three largest Mainline customers and largest Canadian local distribution companies – Enbridge Gas Distribution Inc. (Enbridge), Union Gas Limited (Union) and Gaz Métro Limited Partnership (Gaz Métro). These three companies were referred to as the Market Area Shippers (MAS) during the proceeding.

Following receipt of the application, the Board initiated a comment process among TransCanada shippers and stakeholders. At the conclusion of the comment process, the Board found that it could not approve the Settlement as a contested settlement under the Board's Settlement Guidelines. This letter is contained in Appendix IV.

The Board indicated its willingness to treat the Settlement as a common position of the parties to it (*i.e.* TransCanada and MAS) in a contested tolls application, which TransCanada agreed to on 14 April 2014.

The Board issued a Hearing Order on 9 May 2014, setting the application down for an oral public hearing. The oral portion of the hearing took place in Calgary over 12 days in September 2014.

There were 33 intervenors and 4 commenters granted standing in the process.

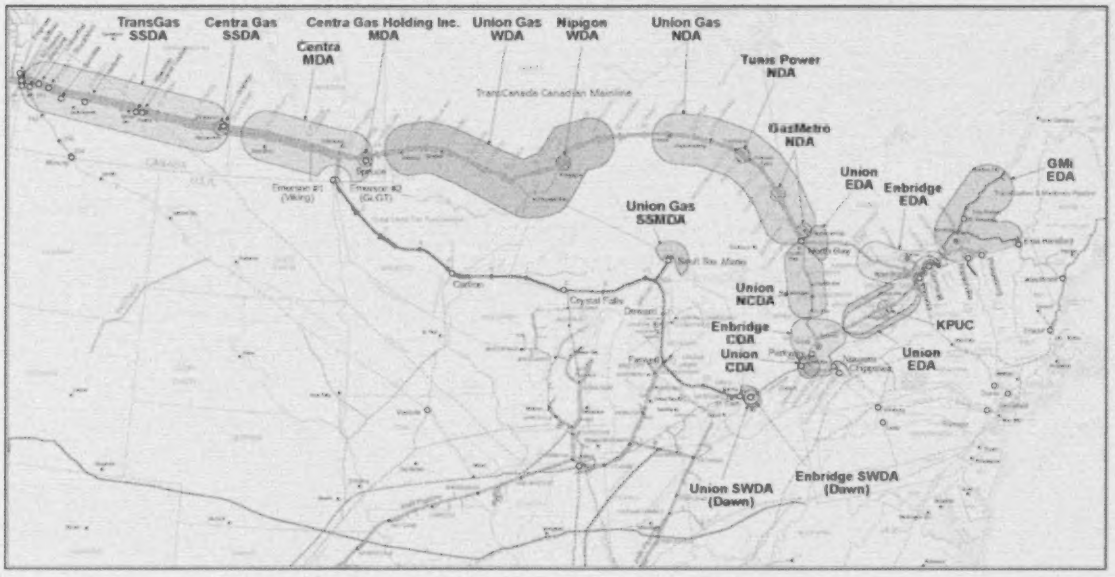
1.2 The Mainline

TransCanada owns and operates the Mainline, which is a high-pressure natural gas transmission system that extends from Empress, Alberta (near the Saskatchewan border) across Saskatchewan, Manitoba, and Ontario and through a portion of Québec. The Mainline connects to various downstream Canadian and international pipelines.

Currently for operational and depreciation purposes, the Mainline is comprised of three geographical segments, each consisting of multiple lines. The three segments are referred to as the Prairies segment, the Northern Ontario Line (NOL) and the Eastern Triangle. The Prairies segment commences at Empress, Alberta and extends eastward to a point near Winnipeg, Manitoba. The NOL commences at Winnipeg and extends eastward to a point near North Bay, Ontario. The Eastern Triangle commences at North Bay and extends southward to a point near Toronto, Ontario, and eastward, to a point near Ottawa, Ontario. These two points are connected by a section of the Eastern Triangle, called the Montréal line, which commences near Toronto and extends to a point near Montréal, Québec. Collectively the Prairies Line and the NOL are also referred to as the Western Mainline.

In addition, the Mainline integrated system includes contractual entitlements (called Transportation by Others (TBO) agreements) used to transport natural gas on the Great Lakes Gas Transmission Company (GLGT) system from Emerson, Manitoba to St. Clair, Michigan; on the Union system from Dawn to Parkway and to Kirkwall, all in Ontario; and on the TQM System from St-Lazare to St-Nicholas and East Hereford, all in Québec. GLGT and TQM are affiliates of TransCanada. See Figure 1-1 for a map of the Mainline.

Figure 1-1 TransCanada Mainline



From the receipt point at Empress, the Mainline integrated system can transport up to approximately 7 billion cubic feet per day (Bcf/d) (198.3 $10^6 m^3/d$) of Western Canada Sedimentary Basin (WCSB) gas to markets. From receipt points located in Manitoba and Ontario, the Mainline also transports natural gas from other production basins, such as the Appalachian basin, to markets.

1.3 Background

1.3.1 RH-003-2011 Decision

In September 2011, when TransCanada made the RH-003-2011 application, the Mainline was in an unprecedented position: contracting practices on the Mainline had dramatically shifted from annual firm service to discretionary services (interruptible transportation (IT) and short term firm transportation (STFT)), shale gas production from the United States had begun competing with volumes from the WCSB, which itself was seeing some declines in production; and changes in the demand for WCSB gas were occurring. The Mainline faced rapidly declining throughput and concomitant substantial increases in tolls over a short period of time.

The RH-003-2011 proceeding included 72 days of oral public hearings and involved the substantive participation of many Mainline stakeholders. In March 2013, the Board released its decision in the RH-003-2011 proceeding.

The RH-003-2011 Decision reflected the Board's view that TransCanada bore the responsibility to ensure the Mainline's economic viability, to address the underlying competitive reality it operated in, and to meet market forces with market solutions. TransCanada could not look to the Board to shield it from the risks it was facing but could reasonably expect to have the tools available to allow it to respond to these risks.

The RH-003-2011 Decision included the following features:

- It fixed Mainline firm transportation (FT) tolls from 1 July 2013 to 31 December 2017 (Compliance Tolls).
- A long-term adjustment account (LTAA) and a toll stabilization account (TSA) were created as the only two deferral accounts on a go-forward basis.
- TransCanada was granted virtually unlimited discretion to set bid floors for discretionary services with the intention that this would help it maximize Mainline revenues. In the Board's view, this greater discretion in setting bid floors was to provide TransCanada the opportunity to recover the costs of its capacity, during the period of time in which its capacity is used, from those who use it.
- The Board delineated the circumstances (off-ramps) that it expected would justify a new tolls application for the Mainline before 31 December 2017. The off-ramps were defined as: (1) the TSA balance is approaching, and is expected to reach, one-ninth the size of rate base; (2) TransCanada expects that the TSA balance will become unrecoverable; (3) the negative TSA balance is nearly, and expected to be, eliminated prior to the 2017 toll year; or (4) TransCanada disposes of or repurposes significant assets.
- The RH-003-2011 Decision reflected an expectation, based on TransCanada's throughput forecast, that TransCanada would under-recover its revenue requirement initially and over-recover its revenue requirement in the later years, with the net result that the fixed tolls would recover the Mainline's revenue requirement over the fixed toll period.

1.3.2 Developments Following the RH-003-2011 Decision

1.3.2.1 Changes in the Natural Gas Markets

TransCanada submitted that due to ongoing changes in the natural gas market, there was a need to evolve from the RH-003-2011 decision model. TransCanada submitted that, in the period following the RH-003-2011 Decision, there was great pressure to accommodate the transportation of new and existing sources of supply, particularly of growing production of Marcellus and Utica shale gas, via short-haul Mainline transportation. However, in the context of a fixed tolling model implemented by the RH-003-2011 Decision, a Mainline expansion to facilitate conversion from long-haul transportation of WCSB gas to short-haul transportation would not be economic. TransCanada submitted that under the Compliance Tolls, TransCanada had a disincentive to expand Mainline facilities from long-haul to short-haul transportation, because facilitating such a shift would reduce revenues. If investments were made to convert long-haul transportation to short-haul transportation under the Compliance Tolls, there would be a significant shortfall in net revenues in the TSA accumulated by the end of 2017.

MAS submitted that without access to the diversity and cost-competitiveness of the Marcellus and Utica supply, the Ontario and Québec economies would be at a disadvantage against competitors that have access to lower cost energy. Market access was critical in providing Ontario and Québec consumers a choice of natural gas supply sources. Due to statutory obligations to provide utility service, MAS submitted its members were obligated to provide secure, reliable and cost-competitive natural gas supply. MAS illustrated that in December 2012, the *Régie de l'énergie* of Québec approved the shift from Empress to the Dawn hub as the natural gas supply source for Québec users. In January 2014, the Ontario Energy Board approved approximately $1 billion of facility expansion projects within the MAS franchises to provide incremental capacity to transport natural gas to the Mainline within the Eastern Triangle. According to MAS, these decisions from two provincial regulators served to demonstrate the importance of providing market access to gas users in Ontario and Québec in order for these economies to benefit from the opportunities that the North American natural gas market provided. MAS submitted that its members could not meet their statutory obligations to serve their customers without a corresponding willingness by upstream providers, such as TransCanada, to serve them.

1.3.2.2 Regulatory and Civil Proceedings

TransCanada submitted that the RH-003-2011 Decision was followed by uncertainty and tension over access to the Mainline and Mainline cost recovery. The disagreements led to a number of litigious proceedings, including the filing of a section 71 application to the NEB by Gaz Métro and Union, as well as TransCanada filing in the Ontario Superior Court for an order that Enbridge comply with an earlier concluded Memorandum of Understanding. In the views of both TransCanada and MAS, this created uncertainty and paralysis in the Mainline gas transportation market.

1.3.2.3 Development of the Settlement

Potentially faced with years of adversarial litigation before the Ontario Energy Board, the NEB and the Ontario Superior Court, along with the associated delays and expenses, TransCanada submitted that MAS and TransCanada were motivated to find a solution. Regulatory and judicial proceedings provided impetus for the settling parties to resolve matters through negotiation.

On 10 September 2013, these settling parties concluded a Settlement Term Sheet that set out all of the material terms of the settlement. The Term Sheet was legally binding until the parties entered into the Settlement on 31 October 2013. The Settlement term runs from 31 October 2013 to 31 December 2030.

There were two amendments to the Settlement, on 15 November 2013 and 13 December 2013, both of which addressed concerns raised by stakeholders who were not part of the original negotiations that led to the Settlement Term Sheet.

1.3.3 Overview of TransCanada's Application

TransCanada put forward its application as a means to facilitate the investment required to promote the development of natural gas infrastructure in Canada, meeting the immediate demands for facilities in the Eastern Triangle while preserving TransCanada's ability to recover costs on the Mainline. The application introduces a wide range of changes to the Mainline in its tariff and tolling structure.

The application relies on a number of high level principles to facilitate its outcome. The first is that it geographically segments the Mainline for tolling purposes, separating the Eastern Triangle rate base and cost of service from the NOL and Prairies Line rate base and cost of service. It seeks approval of rolled-in tolling for new capital expansions in the Eastern Triangle. Then, on a segmented basis, it uses the fixed tolls established in the RH-003-2011 Decision as the starting off point for a three-step adjustment that TransCanada says is calculated to recover the estimated costs of the Mainline, including additional facilities to be built to add incremental short-haul transportation capacity in the Eastern Triangle. Embedded in the tolls calculations is a temporary transitional Bridging Contribution meant to assist TransCanada with recovery of its costs incurred between 2015 and 2020 for expansion facilities in the Eastern Triangle. This contribution is paid by all segments: the Prairies segment and NOL through to 2020; for the Eastern Triangle, it is amortized through to 2030. By the end of 2020, the proposed framework in the application completely insulates Eastern Triangle shippers from costs of the Western Mainline, unless they continue to use it. Overall, TransCanada's proposed tolls, which are to be set for six years (subject to re-evaluation during the 2018 to 2020 toll review discussed in Chapter 8), increase tolling levels set in the RH-003-2011 Decision by 52% for Eastern Triangle short haul, 18% for Eastern Triangle long haul, and 12% for all others.[1]

Whereas the RH-003-2011 Decision had two deferral accounts, the LTAA and the TSA, the application redefines the LTAA and eliminates the TSA. The newly-defined LTAA will capture revenue excess or shortfalls to the revenue requirements. The concept is that a negative balance in the LTAA would be disposed of through an addition to rate base and amortized at the average annual depreciation rate.

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[1] In Undertaking 7, TransCanada provided updated costs and tolls resulting in a slight change to these percentages.

Any remaining balance in the LTAA at the end of 2020, by the terms of the application, is to be recovered in Eastern Triangle tolls. The application also sees TransCanada making an after-tax $20 million annual contribution to the Mainline revenue requirement from 2015 to 2020. The application also reduces the return on equity (ROE) of 11.5 per cent approved in the RH-003-2011 Decision to 10.1 per cent and pursuant to an incentive formula, the applied-for ROE can fluctuate between 8.7 and 11.5 per cent depending on the net revenue.

The application seeks to preserve the discretion the RH-003-2011 Decision granted TransCanada for bid floor pricing for discretionary services. It contains tariff revisions including a five-year term-up provision for firm transportation shippers desiring to retain renewal rights if $20 million or more of new facilities are required. Another revision is the introduction of a minimum of no more than a 15 year contract term for shippers requiring new facilities that convert demand from existing long-haul to short-haul services. It also introduces new services for enhanced load balancing and summer storage.

The application relies on a number of contractual commitments between settling parties, commitments over which the Board has no jurisdiction to enforce but would need to rely upon in order to comprehensively evaluate whether the resultant tolls are just and reasonable and not unjustly discriminatory. These include: TransCanada will build the required facilities needed in the Eastern Triangle, MAS members have committed to retaining long-haul service on the Mainline at least until the end of 2020 and not to bypass the Mainline, the settling parties agreed to withdraw from the various regulatory complaint and civil litigation proceedings they had started, the parties committed to supporting one another's regulatory applications required for facility approval (save for Energy East), amongst many others.

Chapter 2

New Services

2.1 Contract term for expansion facilities

Views of TransCanada

TransCanada proposed that new requests for firm services that require expansion facilities would require a minimum contract term of no more than 15 years commencing on the in-service date of the expansion facilities. This minimum term requirement would be specified in the Transportation Access Procedures and applicable toll schedules of the tariff. TransCanada submitted that a minimum contract term of 15 years for new expansions is increasingly common across North America.

Views of Participants

No participants expressed any concerns with the contract term for expansion facilities.

2.1.1 Views of the Board

Decision

The Board finds that the proposed provision aligns with industry standards and is reasonable. The Board approves a minimum contract term of no more than 15 years for expansion facilities as applied for.

2.2 Other service changes

2.2.1 Diversion and alternate receipt point rights

Views of TransCanada

Diversions and alternate receipt points are features of certain firm transportation contracts, and have a service priority above interruptible transportation. Diversions can be nominated to delivery points downstream of the contracted receipt point. Alternate receipt points can be nominated at points between the contracted receipt and delivery points. An incremental toll may be charged for the extra distance if the nominated path is longer than the contracted path. TransCanada proposed minor changes to the matrix of eligible diversion and alternate receipt point locations by contract path and submitted that the changes are consistent with the existing tariff provisions.

Views of Participants

No participants expressed any concerns with the diversions and alternate receipt point changes.

2.2.2 Modified delivery areas and new delivery locations

Views of TransCanada

TransCanada proposed changes to two distributor delivery areas (DDA) and the establishment of new delivery locations. Effective 1 November 2015, the Enbridge central delivery area (CDA) would be modified. The Parkway-Enbridge meter station would be removed from the Enbridge CDA and placed within a new DDA called the Enbridge Parkway CDA. The remaining Enbridge CDA meter stations would continue to reside within the Enbridge CDA. The modification would facilitate the movement of gas from locations such as Niagara Falls and Chippawa directly to the Enbridge Parkway CDA. Shippers who hold contracts to the Enbridge CDA would go through a one-time contract election process before 1 November 2015 to determine how they wish to split their contract quantities between the Enbridge CDA and the new Enbridge Parkway CDA.

Union is seeking provincial regulatory approval to construct its proposed Burlington Oakville pipeline to be in service 1 November 2016. TransCanada proposed that effective 1 November 2016 the Union CDA would be modified. The current Union CDA consists of five meter stations: Parkway-Union, Bronte, Burlington, Hamilton Gate, and Nanticoke. The Parkway-Union, Bronte and Burlington meter stations would be removed from the Union CDA. The Bronte and Burlington meter stations would form a new DDA called the Union East Central Delivery Area (Union ECDA), and the Parkway-Union meter station would become a new standalone delivery location called the Union Parkway Belt. The remaining Union CDA meter stations, Nanticoke and Hamilton Gate, would continue to reside within the Union CDA. Shippers who hold contracts to the Union CDA would go through a one-time contract election process before 1 November 2016 to determine how they wish to split their contract quantities between the Union CDA, the Union ECDA and the Union Parkway Belt delivery point.

The Union Parkway Belt meter station is an interconnection point between the TransCanada Mainline and Union's transmission system, and functions differently than a typical meter station serving a market within a distributor delivery area. The creation of the standalone Union Parkway Belt delivery point will more accurately reflect the function of this point. Table 2-1 provides the distance and tolls between the existing receipt and delivery points in the Union CDA. Table 2-2 provides the same information for the modified receipt and delivery points.

Table 2-1 Prior to 1 November 2016

Receipt Point	Delivery Point	Distance (Km)	Proposed 2015-2020 Toll ($/GJ/d)
Union Parkway Belt	Union CDA	29.98	0.1536

Table 2-2 After 1 November 2016

Receipt Point	Delivery Point	Distance (Km)	Proposed 2015-2020 Toll ($/GJ/d)
Union Parkway Belt	Union CDA (Amended)	61.02	0.1778
Union Parkway Belt	Union ECDA	11.52	0.1393
Union Parkway Belt	Union Parkway Belt	0	0.1303

Views of Participants

No participants expressed any concerns with the modified DDAs and new delivery locations.

2.2.3 Summer storage service

Views of TransCanada

Summer storage service is a new biddable discretionary service proposed by TransCanada to facilitate the flow of gas from Empress to storage locations in the Union southwestern delivery area (SWDA) and Enbridge SWDA in the summer period. Many characteristics of the summer storage service would be similar to those of interruptible transportation service. TransCanada proposed the bid floors for the summer storage service be set no greater than 100 per cent of the daily equivalent FT toll for the applicable path. This service would be available during summer periods from the later of 1 April 2015, or six months after NEB approval of the application, until 31 October 2020.

Views of Participants

No participants expressed any concerns with the summer storage service.

2.2.4 Enhanced market balancing

Views of TransCanada

Enhanced market balancing service was proposed by TransCanada to allow shippers to effectively balance their market requirements through the use of eight nomination windows on the day. Enhanced market balancing would have features similar to storage transportation service but would not be linked to long-haul transportation. TransCanada submitted that enhanced market balancing would be responsive to the evolution of the market toward accessing gas supplies located in closer proximity to domestic markets and trading hubs. TransCanada proposed a toll for this service equal to 110 per cent of the FT toll for the applicable path.

Views of Participants

No participants expressed any concerns with the enhanced market balancing service.

2.2.5 Views of the Board

Decision

The Board finds that the new services will offer additional options for shippers under reasonable terms and conditions, and therefore approves the new services as applied for.

2.3 Long-Haul to Short-Haul Conversion

Views of TransCanada

TransCanada submitted that Mainline shippers with long-haul contracts will have the option at any time during the term of their long-haul contract to convert all or a portion of their long-haul contract to a short-haul contract while maintaining the same delivery point.

TransCanada submitted that any loss of revenues resulting from the long-haul to short-haul conversion will not be used to assess the viability of new or additional pipeline facilities required to provide for the long-haul to short-haul conversion.

TransCanada submitted that the long-haul to short-haul conversion was subject to each MAS member, during the period of 1 January 2015 to 31 December 2020, holding minimum contract quantities of not less than 265 TJ/day for Enbridge, 85 TJ/day for Gaz Métro and 85 TJ/day for Union.

On 29 November 2013, TransCanada initiated a new capacity open season (2016 NCOS) for new firm transportation service on the Mainline, including requests for conversion of long-haul contracts to short-haul contracts, with an in-service date of 1 November 2016 or as soon as possible thereafter. The 2016 NCOS closed on 15 January 2014.

TransCanada submitted that in its 2016 NCOS it received bids to convert 68 TJ/d of the eligible 1,229 TJ/d of long haul-contracts to short-haul contracts. TransCanada subsequently executed Precedent Agreements with shippers for 63 TJ/d of long-haul to short-haul conversion. TransCanada advised that 1,035 TJ/d remained eligible for conversion in a future open season.

TransCanada submitted that in the absence of a conversion mechanism, a shipper intending to shift from long-haul to short-haul service could enter a new contract for short-haul service and allow its long-haul contract to expire. However, when new facilities are required for new short-haul service, there is uncertainty about the specific in-service date of the new facilities and the start date of the new contract. To address this uncertainty, the shipper would have the choice of contracting long-haul until the expected start date of the short-haul contract, and risk having a shortage of firm capacity if the start date is delayed, or contracting long-haul service past the start date of the new short-haul contract at additional cost. In addition, there may be insufficient capacity in the end-market to support both long and short-haul contracts simultaneously requiring additional facilities for a very short period. With the conversion mechanism, the long-

haul contract is converted and becomes a short-haul contract on the date the new facilities are in service, which provides certainty of timing to shippers for the short-haul capacity.

Views of Participants

Alberta NorthEast Gas, Limited (ANE) did not support TransCanada's long-haul to short-haul conversion. ANE submitted that an orderly transition from long-haul to short-haul service should be considered. ANE argued that there was no reason to raise tolls as a prerequisite to provide existing long-haul shippers with a reasonable opportunity to convert to short-haul service. To mitigate toll impacts, ANE proposed an orderly transition, such as 20 per cent annually rather than all at once, and a requirement that adequate levels of long-haul service be retained.

Specifically, ANE recommended that long-haul shippers be afforded the opportunity to convert up to 20 per cent of long-haul volumes to short-haul per year effective on 1 November of 2016, 2017 and 2018. The remaining 40 per cent could be converted if TransCanada repurposed assets and sufficient net benefits were available to offset the revenue impacts of additional conversions. In ANE's view, this approach represented a reasoned pace of conversion, providing converting shippers with measurable benefits, while preserving the appropriate level of tolls.

TransCanada Reply

TransCanada submitted that ANE's phased approach to long-haul to short-haul conversion should be rejected, because a phased transition would not meet the market demand for more short-haul transportation. In TransCanada's view, the implementation of the ANE proposal would negatively impact the tolls and tariff terms described in the Settlement and put into jeopardy the commitments made by MAS.

2.3.1 Views of the Board

Decision

The Board accepts the long-haul to short-conversion as applied for by TransCanada. The Board did not find the proposed 20 per cent annual transition to be a workable or fair model for the conversion of long-haul to short-haul transportation on the Mainline.

Chapter 3

Contract renewal provisions

3.1 Term-Up Provision

Views of TransCanada

TransCanada proposed that if it determines expansion facilities are required, with an estimated cost exceeding $20 million, it would give notice of this to all shippers with existing FT contracts, who could be affected by the design of the expansion facilities. Within 60 days, the shipper would have the option to extend the term of all or a portion of their applicable contract quantity for an additional period such that their new contract expiration date would be at least five years after the expected in-service date of the expansion facilities, and would retain their renewal rights. If a shipper did not elect to extend its contract term within 60 days, the contract would expire at the end of its existing term. TransCanada argued that the minimum five-year contract term extension for existing shippers in the expansion facility area provides it with a minimum level of commitment to the system it needs to rationalize infrastructure additions and proceed with expansion facility efforts.

In response to information requests, TransCanada submitted that the term-up provision would be invoked for two projects. For the 2016 Mainline Expansion Project, all contracts that originate at St. Clair, Dawn, Niagara, Chippawa, Kirkwall and Parkway to delivery points east of Maple would be subject to the term-up provision. For the Eastern Mainline Expansion, all contracts with deliveries to Cornwall, East Hereford, Enbridge eastern delivery area (EDA), GMIT EDA, Iroquois, KPUC EDA, Napierville, Philipsburg and the Union EDA would be subject to the term-up provision, with the exception of contracts with receipt at Iroquois.

Views of Participants

ANE submitted that under TransCanada's proposal, invoking the term-up provision could result in TransCanada earning annual revenues that potentially exceed the revenue requirement impact of the $20 million expansion by 100 times or more, and that have a net present value of a five-year expansion that could approach $1.0 billion or more. ANE submitted that TransCanada's proposal fails to establish any nexus between the size of a project and the volume of service or revenue impacts to shippers that would be required to term-up. ANE noted that TransCanada does not intend to seek Board approval for its determination of which contracts are subject to term-up prior to issuing notices to customers.

ANE shippers depend on an orderly renewal process in order to manage their portfolio risks, and renewal provisions are an essential element of FT recourse service. If TransCanada issued an early term-up notice two to four years in advance of the effective date of a project and shippers had to extend service for a minimum of five years after the expected in-service date of the project, this would equate to an extension of between seven and nine years. Exposure to an early renewal decision provides shippers with little ability to consider alternative options to a renewal that may extend service for up to nine years from the current date.

ANE submitted that the proposal exposes ANE shippers to an overly-long contract renewal and shifts the risks of operating a pipeline onto shippers. Moreover, the impacts on shippers that are required to extend service that far in advance could result in reduced Mainline utilization and a net revenue loss to TransCanada to the detriment of other FT shippers.

ANE submitted that the application seeks to introduce something similar to the Early Long-Term Renewal Option (ELTRO) concept rejected in the RH-001-2013 Decision. In that proceeding, ANE proposed extending the renewal time for firm contracts from six months to two years in order to assist TransCanada in system planning. ANE agrees with the Board's reasoning for substantially increasing the notice period for renewals from six months to two years, but retaining the one-year renewal as indicated in RH-001-2013 Decision. These changes provide TransCanada with substantial advance notice regarding renewals compared with the previous six-month notice period.

According to ANE, in the RH-001-2013 Decision, the Board cited specific concerns with a general early renewal provision and indicated that TransCanada should instead propose such a provision on a project-specific basis if it felt that it was necessary. Moreover the Board specifically addressed circumstances related to the Eastern Mainline Project related to the Energy East Project. The Board's views regarding general renewal provisions as it pertained to its rejection of TransCanada's ELTRO are equally relevant to its current proposal, which ANE says suffers from the same flaws and should be rejected.

TransCanada Reply

In response to ANE's concerns, TransCanada submitted that the term-up provision establishes clear and transparent criteria, including a defined threshold when the provision would be invoked, a five year minimum contract term to maintain renewal rights, and a 60-day election period. TransCanada asserted that the codification of these transparent criteria is responsive to the concerns stakeholders had with ELTRO.

TransCanada believes that the Canadian public interest is best served by ensuring the rational development of Mainline infrastructure for the benefit of those who have committed to relying on the Mainline over the long-term, such as MAS. TransCanada submitted that the interests of the Mainline and of its long-term shippers far outweigh the individual interests of ANE with respect to the term-up provision.

3.2 Views of the Board

The Board notes that TransCanada has been making efforts to manage the Mainline and respond to shippers' requests to contract for more short-haul transportation to access the Dawn hub and new gas supplies from the Marcellus and Utica basins. The transition to this new regime causes a great deal of uncertainty and would require new facilities to be built. The Board finds that additional information will enable TransCanada to navigate this transition more smoothly, and to build less redundant infrastructure that could become unnecessary in the first few years of operation if existing shippers were to stop shipping on the Mainline. The Eastern Triangle is highly utilized and demand for capacity exceeds the existing infrastructure. In these circumstances it is economically efficient for capacity to be awarded to those who value it most. For these reasons, the Board approves TransCanada's proposed term-up provision.

The Board recognizes that TransCanada is likely to issue term-up notices for one or more proposed Mainline projects soon after the requested term-up provision comes into effect. The Board recognizes that 60 days is a relatively short amount of time for some shippers to make decisions for contracts that extend several years into the future. Accordingly, the Board expects TransCanada to give shippers more than 60-days' notice whenever possible. Shippers who require more than 60 days to make such decisions will need to begin their decision-making prior to the term-up provision notice being issued by TransCanada. Accordingly, the Board has decided that the term-up provision will come into effect on 30 March 2015. If TransCanada issues a term-up notice on that date, shippers would have to make contracting decisions by the end of May 2015. If this scenario materializes, shippers will have had five months to prepare for this decision. The Board finds this to be reasonable. In general, the Board supports TransCanada communicating to shippers as early as possible which particular paths may be subject to term-up provisions in the near future.

Although the Board is approving this general provision, future Board panels considering specific projects will have unfettered discretion in determining just and reasonable tolls and will consider the terms and conditions of service set out in the tariff as they relate to those projects. The Board notes that TransCanada expressly requested issues related to Energy East not be considered in this proceeding and, accordingly, expects that the issue of the treatment of replacement gas facilities for Energy East will be fully considered by the Board at that time.

Decision

The Board approves TransCanada's proposed term-up provision. The term-up provision will come into effect on 30 March 2015.

Chapter 4

Pricing of Discretionary Services

4.1 Pricing Discretion

Views of TransCanada

TransCanada applied for the continuation of pricing discretion established in the RH-003-2011 Decision and submitted that its application relies on this.

TransCanada argued that the factors that led the Board to implement pricing discretion in the RH-003-2011 Decision continue to apply and that maintaining pricing discretion remains a necessity. Absent pricing discretion, shippers would return to the contracting behaviour observed before implementation of the RH-003-2011 Decision, where they relied on IT and STFT to meet firm requirements and paid only a fraction of the annual cost of the Mainline capacity.

TransCanada submitted that pricing discretion has functioned as intended by the Board, because shippers who require guaranteed access to the Mainline have reverted to FT service. For the six months prior to the implementation of RH-003-2011 Decision, firm contracts on the Mainline totaled approximately 4,900 TJ/day, including approximately 1,100 TJ/day of long-haul contracts. Since the decision's implementation, firm contracts on the Mainline have increased, nearing a total of 7,800 TJ/day at the end of March 2014, including long-haul contracts exceeding 3,500 TJ/day.

TransCanada submitted that while IT quantities initially declined, as expected with the elimination of risk alleviation mechanism (RAM) on 1 July 2013, the quantities of gas transported under both IT and STFT have since steadily increased. In TransCanada's view, this confirmed that IT and STFT continue to provide the market with a competitive alternative.

TransCanada stated that it had responded to pricing signals in the market and the price for IT and STFT varied. When the value of capacity was high, TransCanada sold both IT and STFT above the applicable FT toll. At other times, TransCanada was able to capture discretionary opportunities by discounting the bid floor of IT below the FT toll.

TransCanada submitted that for STFT service, the bid floors posted during the 1 July 2013 to 31 March 2014 period were 100 per cent to 4,000 per cent of the FT toll. STFT sales were for various contract durations, ranging from 7 days to 212 days, and occurred at levels between 100 per cent and 3,300 per cent of the FT toll, with a volume-weighted average of 210 per cent. Approximately 60 per cent of the STFT quantity sold was contracted above the posted bid floor, and approximately 23 per cent of the STFT sales occurred at levels exceeding 200 per cent of the FT toll. Typically, higher STFT tolls relative to the FT toll were associated with shorter contract durations and shorter paths.

For IT service, the bid floors set during the 1 July 2013 to 31 March 2014 period were in the range of 15 per cent to 5,500 per cent of the FT toll. Daily IT sales during this period averaged approximately 280 TJ/day and exceeded 465 TJ/day over the November 2013 through March 2014 winter period. A peak of approximately 2,200 TJ/day of IT sales was reached on 27 January 2014. IT sales occurred over the entire range of bid floors posted (15 per cent to

5,500 per cent of the FT toll), with the volume-weighted average equating to 543 per cent. Approximately 22 per cent of IT sales were sold at a discount to the FT toll, while 21 per cent of the IT sales were at 500 per cent or more of the FT toll. Approximately 18 per cent of IT sales were at levels above the posted bid floor.

TransCanada argued that the overall results confirm it was successful in preserving the value of FT and optimizing overall revenue. The fact that shippers bid up to 3,300 per cent of the FT toll for STFT and 5,500 per cent of the FT toll for IT confirmed that imposing a cap on the bid floors would unnecessarily constrain TransCanada's ability to generate revenues. Furthermore, a cap on bid floors would diminish the incentives intended in the RH-003-2011 Decision of inducing shippers who need guaranteed access to the Mainline throughout the year to pay for the full annual costs related to that capacity.

TransCanada argued that Mainline shippers have benefitted and will continue to benefit from maintaining pricing discretion since the vast majority of incremental net revenues is credited to shippers.

TransCanada submitted that the price it can obtain for IT and STFT has been and will remain constrained by the secondary market. TransCanada stated that the more than tripling of long-haul FT contracts since implementation of the RH-003-2011 Decision increased the transportation capacity available to be resold in the secondary market. TransCanada submitted that its sale of IT service was also constrained by shippers using diversions. Despite the transportation value exceeding IT bid floors on many occasions during the 2013-2014 winter, shippers rarely bid for IT to eastern markets, because IT nominations would not be successful.

TransCanada submitted that the availability of FT service as recourse to discretionary services would be maintained under the application, and would be enhanced, because it would commit TransCanada to invest in new facilities. TransCanada submitted that pricing discretion should be maintained on all paths, including those paths where there is no FT available. On paths where FT capacity is not available, a shipper can request new FT service. TransCanada emphasized that shippers with firm requirements should not rely on the availability of IT to meet firm requirements, and that shippers need to plan ahead to meet incremental firm service requirements.

TransCanada identified several alternatives to IT and STFT in the secondary market: a shipper can purchase either firm or discretionary capacity, including diversion rights, directly from an existing shipper; capacity could be obtained through assignment from an existing shipper on a temporary or permanent basis; a shipper can use an over-the-counter broker to purchase gas at a specific location; a shipper may be able to purchase service through a local distribution company (LDC) if the shipper is located in an LDC franchise area; and, a shipper can purchase gas at a specific location directly on an exchange such as NGX or ICE.

TransCanada emphasized that forecast FT contracts and discretionary miscellaneous revenue (DMR) reflected in the proposed tolls for the 2015 to 2020 period relied on the continuation of pricing discretion. Absent this discretion, the revenues expected to be derived by TransCanada under the proposed tolls would be well below the Mainline revenue requirement.

TransCanada also submitted that absent pricing discretion, shippers would revert to using discretionary services to meet their firm requirements, even with the proposed term-up. First, TransCanada submitted that the term-up could only be invoked in situations where expansion

facilities were required. The term-up will have no impact on shippers' incentive where no expansions are anticipated or for specific paths not needing expansion facilities. Second, any shipper who chose not to extend the term of its contract by five years, but whose contract expires after the new facilities are in place, may revert to IT and STFT upon expiry of its FT contract. In addition, shippers who firmed up for five years may revert to using discretionary services at the end of the five-year period.

Views of Participants

ANE

ANE supported maintaining pricing discretion, subject to availability of recourse FT, because it led to an increase in FT contracting and contributed to strong IT and STFT revenues. In ANE's view, the increase in FT contract volumes helped to increase the Mainline's revenue stability, reduced upward pressure on the level of tolls, and ensured that TransCanada recovered a greater proportion of costs from users of its system.

At the same time, ANE stated it was concerned that TransCanada had reaped substantial benefits from the increased revenues attributable to the discretionary pricing flexibility in the form of incentive payments while proposing to delay crediting shippers with any benefit of the excess revenues until after 2020. ANE submitted it was essential that shippers realize the benefits of the improved revenues which have been captured in the TSA, by eliminating the TSA and LTAA balances and reducing the rate base.

BP Canada Energy Group ULC (BP)

BP submitted that the application would reduce TransCanada's business risk, compared to the risk following the RH-003-2011 Decision. BP argued that it lays off utilization risk, primarily to the MAS members, and that the Mainline will therefore revert back to a cost-of-service pipeline. As a result, BP stated that TransCanada will no longer be accountable for how its pricing discretion is exercised and the impact it may have on revenues. BP summarized that this realignment of risk between TransCanada and MAS necessitated a careful re-examination by the Board of the need for unfettered pricing discretion.

BP submitted that all available Mainline capacity should be offered by TransCanada at all times on an as-available basis if shippers are to be able to reasonably manage the risks associated with discretionary pricing. BP expressed concern that there is nothing currently in the tariff requiring TransCanada to do this. If all available FT recourse capacity is not posted on this basis, then there can be no effective check and balance on the bid floor price of available capacity being offered as a discretionary service.

Canadian Association of Petroleum Producers (CAPP)

CAPP stated it did not support the continuation of unlimited pricing discretion for STFT and IT. CAPP argued that the continuation of pricing discretion was not in the public interest, because it would not result in discretionary tolls that are economically efficient or tolls that rationally allow shippers to make the best use of the Mainline. In CAPP's view, TransCanada's practices regarding unfettered price discretion have already led to, and will continue to lead to, inefficient and disruptive tolls.

CAPP stated that although TransCanada had experienced increased FT contracting, and greater than anticipated DMR, since the implementation of the RH-003-2011 Decision, those benefits came at a cost to both the Mainline shippers and the parties who participate in the North American natural gas market. CAPP argued that TransCanada's discretionary pricing behaviour had not been economically efficient because it imposed unnecessary constraints and those constraints drove market prices. CAPP submitted that the price data presented by Dr. Orans showed that market forces no longer determined the NIT price of gas, but rather, the price was driven by TransCanada. It is this control that CAPP believed was inappropriate.

Dr. Orans, on behalf of CAPP, submitted that between July and September 2013, TransCanada increased bid floors on the Empress to Emerson path from $1.00/GJ to $2.50/GJ. As the cost to transport gas between these two markets increased, the price spread between the points also grew. In Dr. Orans' submission, the increase in price spreads between Empress and Emerson had a substantial impact on gas prices at NIT, which decreased from approximately $3.50/GJ to $2.00/GJ during this period. CAPP submitted that the period of 1 July 2013 to 1 October 2013 saw the lowest flows of the last five years from Empress on the Mainline. This occurred in spite of the amount of FT contracting growing during this period to the highest levels since 2010.

Dr. Orans submitted that high spot pricing correlations between various trading hubs in North America for the past five years stand in stark contrast to the pricing correlations observed after the implementation of the RH-003-2011 Decision, primarily between July and September 2013. Historically the NIT market had nearly perfect correlation with many other hubs throughout the United States: these relationships disappeared between July and September 2013. Dr. Orans argued that when markets become disconnected, it is typically an indication of a shortage of pipeline capacity between the two markets. In the case of the divergence of NIT prices from the North American markets between July and September 2013 however, the scarcity of pipeline capacity was not a physical scarcity, but in Dr. Orans' view, a scarcity imposed by TransCanada through its pricing of short-term services. While the Mainline had physical capacity to carry additional gas from the WCSB to eastern markets, TransCanada raised the STFT and IT bid floors to levels that decreased the amount of volume using those services. As a consequence, the NIT and Dawn prices that had been nearly perfectly correlated during 1 January 2008 to 30 June 2013 ($r=0.99$), became almost entirely uncorrelated during 1 July 2013 to 30 September 2013 ($r=0.34$).

Dr. Orans submitted that high bid floors for short-term services did not encourage efficient use of the Mainline. In Dr. Orans' view, a pipeline encouraged economically efficient flows if it offered IT service at a cost between its variable cost and the value of transportation in a competitive market. Whenever short-term prices for transmission services were set at levels that restricted efficient flows, the pipe was performing a form of economic withholding. Dr. Orans submitted that from July to September 2013, TransCanada effectively practiced economic withholding of short-term services and this was done presumably with the goal of forcing shippers to sign FT contracts for capacity they could otherwise obtain through STFT and IT services. CAPP summarized that high pricing of discretionary services added no revenues to TransCanada for recovering costs from those that use the system for short-term transactions, because once a breakpoint was reached, the transaction would not take place. Any positive impacts of increased pipeline utilization and increased transaction volumes were therefore lost.

Dr. Orans submitted that between October and December 2013, TransCanada continued to set bid floors at high levels, but the price spreads between Empress and Emerson decreased. Dr.

Orans attributed this change to the increase in FT-NR contracting, which presumably increased the depth of the secondary market for gas transportation on the Mainline. During this period, it appeared that activity in the secondary market promoted more efficient use of Mainline capacity. Nonetheless, Dr. Orans submitted that TransCanada's reaction to this change in market dynamics appeared to have been very slow, because for nearly two months, bid floors remained at levels above the market value of transportation. Dr. Orans argued that through its failure to respond to the market during this period, TransCanada presumably forfeited the opportunity to earn discretionary revenues.

Between January and March 2014, TransCanada raised bid floors for IT and STFT to levels significantly higher than those in July through December 2013. During this period, much of the United States and Canada experienced record cold temperatures, which caused extreme increases in gas prices at several major market hubs throughout the eastern United States and Canada. Dr. Orans argued that TransCanada's sharp increase in discretionary bid floors between January and March 2014 appeared to be an attempt to maximize revenues by capturing economic rents. Dr. Orans submitted that during this time, TransCanada's pricing behaviour did not encourage efficient use of the Mainline. Dr. Orans argued that notwithstanding the fact that TransCanada's pricing behaviour indicated an attempt to select bid floors that tracked the value of the transportation, it was apparent that not all Mainline capacity was utilized to transport gas from Alberta to eastern markets. Bid floors on some days were set at levels above the price spreads. In Dr. Orans' view, TransCanada's pricing behaviour contributed to the extreme prices in eastern markets, because capacity could have been used to relieve extreme prices in downstream markets.

In response to comments from TransCanada that Centra's and CAPP's positions on pricing discretion and impacts on commodity pricing conflicted, CAPP submitted that the two positions are not inconsistent, but rather reflect observations taken at different points of time. Observations at the low price point (by CAPP) and at the high price point (by Centra) are consistent with the position advanced by CAPP that pricing discretion has had unintended consequences.

CAPP argued that the secondary market does not constrain TransCanada's discretionary pricing, because the secondary market is thin and unavailable when FT shippers fully utilize their contracts.

Dr. Orans submitted that while the secondary market had acted to constrain TransCanada's ability to post high bid floors (or limit their impact) in certain instances, at other times the secondary market had done little to protect the market from high prices for discretionary services. Dr. Orans argued that the depth of the secondary market and its ability to act as a check against monopolistic pricing by TransCanada depended on market conditions. CAPP submitted that when transportation demand exceeded firm contracts, the secondary market was prevented from effectively competing with TransCanada in the pricing of discretionary services, because TransCanada was the only party capable of offering incremental transportation service to meet demand. When firm contracts exceeded demand, the secondary market was able to effectively compete with TransCanada in the pricing of discretionary services. CAPP witnesses summarized that shippers who sign up for FT do so for economic reasons and when demand increases and the market for transportation is tight, shippers will use FT for their own purposes, not resell capacity in the secondary market. CAPP argued that TransCanada was not effectively constrained in the pricing of discretionary services from July to September 2013 and from January to March 2014.

CAPP stated that given TransCanada's ability to price discretionary services on each path uniquely, TransCanada has the ability to price certain paths off the market, while pricing other paths economically. Since the implementation of pricing discretion, TransCanada has priced certain export points at a discount to others, as well as to other delivery areas. The result is that while capacity has been highly utilized on some paths, many other paths have gone largely unused. CAPP argued that TransCanada should not be in the role of a traffic cop on its system because the ability to direct gas to select markets or its affiliates is inappropriate.

Overall, CAPP submitted that to the extent that the Board determines tolls that balance the goals of encouraging economic efficiency and allocating cost recovery, market commodity prices and NIT netbacks are not a concern. However, when a tolling framework prevents otherwise economic transactions from taking place, it fails to promote economic efficiency, and this is not in the public interest. CAPP emphasized that TransCanada's goal is to optimize revenues on the Mainline, at the expense of precluding otherwise economic transactions from taking place. The principle of economic efficiency in setting tolls should be prominent in the Board's deliberations on TransCanada's application.

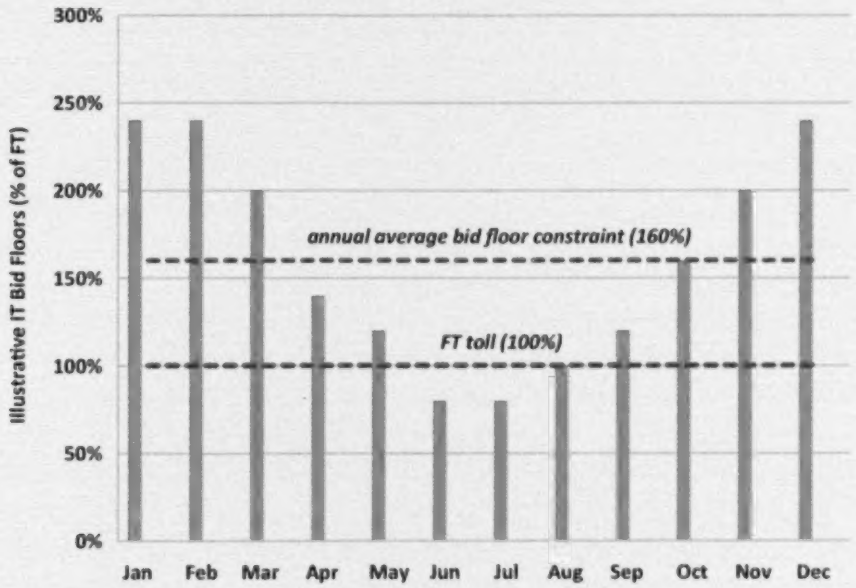
CAPP observed that while forcing parties to make decisions and creating a sense of uncertainty in the market may incent the purchase of FT, it is harmful to the market. CAPP submitted that IT service clears the marginal gas molecule that prices the NIT market. Because the Mainline is the marginal pipeline out of the WCSB, CAPP submitted TransCanada possesses the power to impact the NIT price.

Dr. Orans submitted that the suppression of prices at NIT by approximately $1 per GJ amounted to $1 million dollars in lost revenue to producers per million GJ of natural gas sold into the NIT market. The immediate loss of revenue for gas producers (and corresponding royalties/taxes to the government) and the added uncertainty and volatility in netback prices increased the risk associated with producers' returns on capital and deterred long-term investment.

CAPP witnesses Mr. Thorn and Mr. Cusson submitted that although hedging programs or purchasing FT contracts on the Mainline were all options available to WCSB producers to mitigate NIT volatility, these options were not simple, practical or economic for all producers, particularly for CAPP's smaller members.

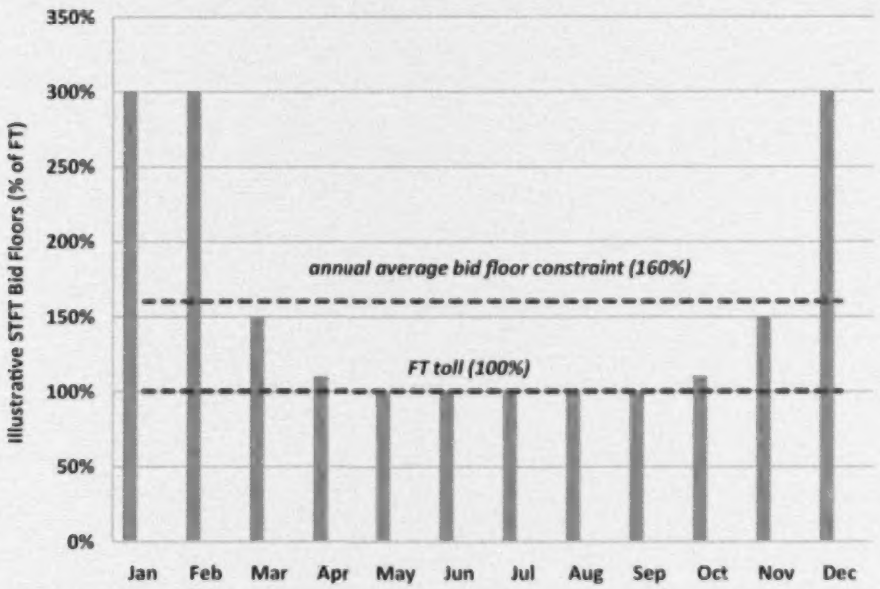
CAPP recommended that the Board impose a limit on the bid floors for IT such that, on an annual basis, the average maximum bid floors for each path would not exceed 160 per cent of the FT toll (see Figure 4-1). According to the CAPP model, by February 15th of each year, TransCanada would select a maximum bid floor for each month of the following gas year whose annual average would not exceed 160 per cent of the FT toll. Prior to each day, TransCanada would select a bid floor for IT services up to that month's corresponding maximum. Available capacity would be allocated to shippers in an auction.

Figure 4-1 Illustrative IT Bid Floors Throughout the Year Under the CAPP Proposal



CAPP also recommended extending the capped pricing structure it proposed for IT to STFT (see figure 4-2). CAPP stated it viewed STFT as the service that most easily substitutes for FT and proposed that the short-term STFT be eliminated in favour of a minimum one month STFT period.

Figure 4-2 Illustrative STFT Bid Floors Throughout the Year Under the CAPP Proposal



Dr. Orans submitted that the CAPP proposal provided TransCanada the flexibility to set bid floors in such a way that met TransCanada's objective of mitigating migration from FT. In the

winter months of the year, during which shippers place a high value on transportation, TransCanada can set tolls at high levels in order to deter shippers with firm needs from using discretionary services. By setting the maximum bid floors for each month ahead of the gas year, TransCanada had the opportunity to send a strong and clear signal to the market to encourage FT contracting.

Dr. Orans submitted that evidence supports CAPP's recommendation that an average limit of 160 per cent is appropriate for interruptible floors, because nearly three quarters of all IT services purchased by shippers were sold at bid floors under 400 per cent.

CAPP submitted that the Mainline's business risk was reduced under the application and that the reduction in risk supported a change to pricing discretion. The implementation of the Bridging Contribution resumed the link between the Mainline's cost of service and its tolls, and therefore reduced the Mainline's cost recovery risk.

In response to TransCanada's position that absent the existing pricing discretion shippers would revert to the contracting behaviour before the RH-003-2011 Decision, CAPP submitted that TransCanada's market was shifting from long-haul transportation to short-haul transportation and that pricing discretion would not shift declining volumes back to long-haul FT. CAPP submitted that based on TransCanada's FT forecast, long-haul volumes will decrease from 2,275,885 GJs/d in January 2015 to 635,585 GJs/d in November 2016. CAPP argued that these volumes were permanently gone and that TransCanada was overstating the future role of pricing discretion.

Mr. Mikkelsen submitted that the majority of forecast FT contracts for 2015 and 2016 were already in place, and therefore TransCanada had limited FT revenue.

Mr. Mikkelsen submitted that TransCanada's Base Case forecast indicated TransCanada would exceed the forecast DMR for the period 2015 to 2020 with IT and STFT tolls set at 200 per cent of the FT toll. Given the ability of the CAPP model to shape the bid floors around an annual average of 160 per cent, Mr. Mikkelsen submitted that TransCanada should be able to achieve average IT/STFT revenue of 200 per cent of the FT toll by effectively using the discretion proposed by CAPP.

CAPP submitted that should the Board not approve CAPP's proposal, or approve TransCanada's application, the Board should still deal with the issue of pricing discretion. Even if the status quo was to remain, CAPP argued that the Board should place reasonable limits on TransCanada's pricing discretion.

CAPP disagreed with TransCanada's submission that CAPP's current position on tolling methodology's impact on producers' netbacks was inconsistent with the position CAPP took in RH-003-2011. CAPP submitted that it proposed limits on pricing discretion because the evidence demonstrated that it has led to unjust and unreasonable tolls.

Centra Gas Manitoba, Inc. (Centra)

Centra submitted that TransCanada's pricing discretion should be constrained due to its harmful effects on commodity prices at downstream hubs.

Centra submitted that during the 2013-2014 winter, natural gas price increases at hubs served by the Mainline were unprecedented. The 2013-2014 winter high day-ahead price at Emerson was

more than 300 per cent of the previous high price, and day-ahead prices exceeded the previous high index price on nearly 20 days. Prices at Dawn also reached new highs that averaged more than 200 per cent of previous highs. Centra noted that these hubs were not experiencing physical constraints.

Centra also submitted that for the 1 January to 31 March timeframe over the 11-year period from 2003 to 2013, a total of 993 days, the Emerson price exceeded the Chicago price by at least $1.00 only once. In contrast, during the same January to March period in 2014, the Emerson price exceeded the Chicago price by more than $1.00 36 times out of 90 days, including 12 times by at least $5.00, and up to a maximum of $10.34.

Despite widespread coincidence of cold weather and low late-winter storage inventory levels across the continent, high prices appeared to have been confined to hubs served directly off of the Mainline or pipeline systems interconnected to the Mainline. Centra also submitted that the long-standing, high degree of correlation of North American gas prices appeared to completely disconnect from prices at AECO during the winter of 2013-2014. This dislocation was not present at hubs not served or not interconnected with the Mainline.

Centra submitted that TransCanada was able to sell approximately 630 TJ/day of FT contracts on the Empress to Emerson path during the three months following the implementation of pricing discretion. The Empress to Emerson IT bid floor during this period was below 300 per cent for all but four days, when the bid floor was set at 311 per cent. No other days exceeded 285 per cent, and the average bid floor was 230 per cent. Centra argued that this demonstrated that bid floors below 300 per cent were sufficient to incent significant FT contracting. Shippers entered into FT contracts, notwithstanding the fact that a large amount of capacity was available and they could have waited to acquire this capacity later.

Centra submitted the Board should cap TransCanada's bid floors in the range of 160 to 300 per cent. Such a limit would allow TransCanada to increase its share of economic rent, without inflating the overall economic rent paid by end-users. Centra submitted that while the pricing of discretionary services within this range would still inevitably have some impact on the secondary transportation market and downstream commodity prices, Centra submitted that the effect would be limited in comparison to the current unlimited pricing discretion.

Mr. Sanderson submitted that based on evidence filed by TransCanada, as well as his experience in the natural gas market, posted bid floors create a ceiling up to which secondary market participants can price their delivered gas to a particular delivery point. Using the Empress to Emerson path as an example, Mr. Sanderson explained that under certain market conditions, particularly during periods of high demand, the secondary market knows it can increase gas prices at Emerson up to TransCanada's bid floor level, because the two are substitutes. Centra submitted that during the 2013-2014 winter, marketers would not sell gas at Emerson until TransCanada posted its bid floor on the Empress to Emerson path, despite the fact that many marketers held FT capacity to Emerson. Centra therefore argued that bid floors lead the market, rather than respond to it.

Dr. Cicchetti stated that in his analysis of the commodity price movements during 2013-2014 winter he found unusual pricing patterns, which in his view, could not be attributed solely to natural market forces.

Dr. Cicchetti performed various regression analyses to test the hypothesis that higher IT bid floors on the Mainline would cause commodity prices to increase at interconnected hubs. Dr. Cicchetti submitted that with extremely high degrees of statistical confidence, he could not reject the hypotheses that: TransCanada's IT bid floor prices affected commodity prices at the same or nearby locations; TransCanada's IT bid floor prices at Emerson affected downstream commodity prices at hubs that TransCanada served directly; and TransCanada's IT bid floor prices at Emerson and Dawn affected commodity prices at other hubs indirectly connected to TransCanada (*i.e.* Niagara, Chicago, Mich Con, and Dominion South). Dr. Cicchetti could on the other hand reject with extreme statistical confidence the hypothesis that TransCanada's bid floor prices at Emerson affected commodity hub prices where TransCanada did not deliver natural gas (*i.e.* AECO/NIT, PG&E Gate, San Juan, Permian, So Cal City Gate, and Leidy).

Overall, Dr. Cicchetti submitted that his regression equations explained about 80 per cent of the variation in commodity prices at Centra Manitoba Delivery Area (MDA), Emerson, Dawn, and Iroquois.

Dr. Cicchetti provided an update to the regression analysis in his evidence that included consideration of weather effects. According to Dr. Cicchetti, the results demonstrated that the addition of his weather variables did not affect his original conclusions that on days and at locations where TransCanada sharply increased the IT bid floor, there were unusual and not otherwise easily explainable natural gas commodity price jumps.

Dr. Cicchetti submitted that pricing discretion may be more powerful than necessary to achieve the shift to FT contracting. A legitimate inquiry would be to determine whether TransCanada could have firmed up sufficient FT revenue with less market disruption and less costs for consumers.

Dr. Cicchetti stated that the Board should adopt a cautious approach going forward. First, the Board should consider limits on pricing discretion. Second, given both high costs on some consumers, and uncertainty related to the necessary degree of discretionary pricing, the Board should reject any extension of discretionary pricing beyond 2017.

Centra emphasized that pricing discretion resulted in shippers such as Centra paying twice: once for the FT capacity on the Emerson to Centra MDA that Centra needs to serve its market and then again when Centra purchases natural gas supply at Emerson which has been impacted by unlimited pricing discretion.

Centra disagreed with TransCanada's position that certain shippers were no longer using diversions only as a tool to mitigate unutilized demand charges (UDCs), but were also using diversions to access high priced markets and backfill firm contractual requirements with IT service if required. Centra advised that it did not face this circumstance. Centra stated that it was never short FT capacity during the 2013-2014 winter, and therefore had excess Mainline capacity every day. Centra argued that the NEB affirmed in the RH-001-2013 Decision that shippers must maintain the ability to divert downstream and mitigate UDCs, and that TransCanada's desire to maximize revenues does not diminish this.

Centra disagreed with Dr. Carpenter's assertion that TransCanada did not have market power for the provision of short-term services, because the effect has not been sustained for a significant period of time, such as one year. Centra also disagreed with Dr. Carpenter's Dawn market concentration analysis and argued that Dr. Carpenter's evidence underestimates the influence of

the Mainline and pricing discretion on the Dawn hub. Centra submitted that there is 2 Bcf/d of capacity on the St. Clair to Dawn path on the Mainline. A maximum of approximately 0.5 Bcf/d was held as FT during the 2013-2014 winter. Centra argued that approximately 1.5 Bcf/d of capacity was available for discretionary services and was therefore subject to pricing discretion, significantly more than the approximately 0.3 Bcf/d of capacity assumed by Dr. Carpenter.

Centra disagreed with TransCanada's argument that Centra's and CAPP's positions on pricing discretion and impacts on commodity pricing conflict. Centra argued that its position is not inconsistent with CAPP's and that while the evidence presented by each intervenor analyzed different periods in time, both concluded that TransCanada's pricing discretion influenced the market.

Industrial Gas Users Association (IGUA)

IGUA stated that while it supported refinements to the application, provided that the incentive for TransCanada to build in the Eastern Triangle was not dismantled, IGUA saw opportunities for improvements in some areas, one of which was limiting TransCanada's pricing discretion.

MAS

MAS supported the retention of pricing discretion established in the RH-003-2011 Decision. MAS stated pricing discretion enabled TransCanada to recover more of the costs of the Mainline from shippers using discretionary services, while preserving the value of FT service and optimizing overall revenues to the benefit of all shippers.

MAS submitted that the application provided shippers with reasonable access to short-haul transportation, thereby providing an additional alternative to discretionary services.

MAS stated it agreed with TransCanada that the continuation of pricing discretion may be subject to further review by the Board in relation to the establishment of tolls for the post-2020 period.

MAS witnesses all agreed with Dr. Carpenter's position that a price leadership model for TransCanada with respect to gas prices at Dawn would not apply, because discretionary services are too small a proportion of the overall market. The Mainline is only one of many pipelines that connect to Dawn.

In response to CAPP's position on pricing discretion, Enbridge and Union stated that if producers do not want to pay discretionary prices for the use of the Mainline, they too can subscribe for firm service and can contribute year round to the recovery of Mainline costs. Enbridge and Union emphasized that whether NIT pricing is affected should not impact the exercise of the Board's discretion to set just and reasonable tolls.

Enbridge and Union acknowledged concerns expressed about the impact of discretionary pricing upon market prices over the past winter and submitted that there were many factors, not one single factor, which resulted in the volatile and elevated prices experienced during an exceptionally cold winter.

Enbridge and Union emphasized that construction of new capacity in the Eastern Triangle was urgently required in order to provide the short-haul FT recourse service which was intended by the Board to help constrain levels of discretionary pricing.

Northland Power

Northland argued that unconstrained pricing discretion was not compatible with a higher recourse toll and elimination of the LTAA as structured in the RH-003-2011 Decision, both of which lowered TransCanada's risk. Northland concluded that if the Board approved the application, pricing discretion should be constrained.

Ontario Ministry of Energy

In light of current market circumstances, the decreased risk that TransCanada would be subject to, and in an attempt to avoid unintended market and customer impacts, the Ontario Ministry of Energy asked that the Board limit TransCanada's pricing discretion to a maximum threshold of 160 per cent. In the alternative, the Ministry requested that the Board impose a 300 per cent cap on pricing discretion.

The Ministry also requested that the Board monitor the level of TransCanada's DMR and related deferral accounts between 2015 and 2020 and measure them against pre-determined thresholds. If the threshold was reached, this should prompt the Board to initiate a review of pricing discretion.

TransCanada Reply

TransCanada stated that the vast majority of Mainline shippers did not oppose the continuation of pricing discretion.

TransCanada argued that its use of pricing discretion did not result in economic withholding or exercise of market power. TransCanada stated that if one were to accept Dr. Orans' definition of economic withholding, TransCanada would be required to post discretionary services at a discount to FT for a substantial majority of time. This would lead to a migration away from FT services, significantly reduce revenues, and undermine the long-run efficiencies the Board sought by granting pricing discretion. Moreover, if this were the standard, most pipelines in North America would be engaged in economic withholding on many days of the year.

TransCanada submitted that the evaluation of flows from Empress since the implementation of pricing discretion shows that economic efficiency had been enhanced. Between 1 October 2013 and 30 June 2014, flows from Empress averaged 3,122 TJ/day. This was significantly higher compared to the same period of the previous year, when the flows from Empress averaged 1,981 TJ/day.

Dr. Carpenter submitted that Dr. Orans' concept of economic efficiency was short-term in nature. Dr. Carpenter argued that given the high fixed cost and low variable cost economics of pipeline investments, long-term contracting of pipeline capacity helped manage business risks faced by pipeline investors. Long-run efficiency would be compromised if existing pipelines that have suffered contract non-renewals and less than full utilization were forced to price short-term services so as to maximize short-term throughput.

Mr. Reed submitted that the focus of Dr. Orans' evidence was only on increasing throughput utilization. Mr. Reed argued that maintaining pricing discretion was consistent with both allocative efficiency (by allocating the discretionary services to those who most value those

services) and productive efficiency (by minimizing the costs of meeting total demand on the Mainline, *i.e.* lowering FT tolls by optimizing overall revenue).

Overall, TransCanada emphasized that pricing discretion was intended by the Board to allow TransCanada to maximize overall Mainline revenues over the long-term, not to maximize Mainline throughput in the short-term. It is over the long-term that the economic efficiency of TransCanada's pricing discretion must be assessed.

TransCanada submitted that the secondary market, including diversions and firm recourse tolls, provides sufficient competitive discipline to TransCanada's pricing discretion.

First, TransCanada submitted that the increased amount of FT contracting has resulted in significantly more available capacity in the secondary market to compete against TransCanada's discretionary services. Second, to the extent there is value in a downstream market, a shipper is able to capture it by utilizing diversions. TransCanada submitted that diversions have proven to be very effective for shippers in capturing market opportunities. The use of diversions represented 11 per cent of system demand from 1 July 2011 to 30 June 2013. This increased to 21 per cent of system demand from 1 July 2013 to 31 March 2014. According to TransCanada, certain shippers were no longer using diversions only as a tool to mitigate UDCs, but were also using diversions to access high-priced markets and backfill firm contractual requirements with IT service.

In TransCanada's view, evidence that competitive constraints have been effective can be observed in the forward markets. Forward markets, which in TransCanada's view are the best predictor of future prices, have not experienced a step change since the implementation of pricing discretion.

Dr. Carpenter submitted that the market for short-term services at Dawn or other major delivery points on the Mainline was not concentrated, therefore the risk that TransCanada had or exercised market power was low. Dr. Carpenter calculated that TransCanada's share of transportation capacity to Dawn, and storage withdrawal capacity at Dawn, was only 6 per cent.

Dr. Carpenter submitted that a price leadership model for TransCanada with respect to the Dawn market would not apply, because TransCanada's discretionary services are too small a proportion of the market. There are several other large diameter pipelines that meet at Dawn that impact Dawn prices, not just the Mainline. Mr. Reed added that the more that TransCanada's pricing discretion is constrained, the more likely it is that pricing behaviour and pricing patterns would be fully predictable.

Mr. Johannson argued that the fact that TransCanada's bid floors are not taken up by the market every time they were set indicates that the secondary market is working. Mr. Johannson submitted that 70 per cent of the offers for short-term services that TransCanada posted had no buyers. Despite this, as was demonstrated by transactions on exchanges and through the use of diversions, it was clear to TransCanada that secondary market activities were occurring.

Mr. Johannson emphasized that TransCanada bid floors are set three hours before the nomination cycle, and that these were one amongst many pieces of information that competitors would use in pricing their own products, either in the secondary market or otherwise.

TransCanada argued that many factors other than pricing discretion played a role in the historic price disconnects at NIT and that many factors other than pricing discretion were likely to have led to the disconnect at NIT during the summer of 2013. First, at the end of winter in early 2013,

Alberta gas storage balances were above the historic average. By the end of June 2013, Alberta gas storage levels were 34 per cent higher than the ten year average of 295 Bcf. Second, the southern Alberta floods of June 2013 constrained gas pipeline export capacity out of the province. Third, the Northern Border pipeline had a planned four day outage, impacting 8 Bcf of supply that would normally flow on it. Finally, the elimination of RAM had a significant impact on WCSB export volumes as RAM credits were mainly utilized to transport gas from Empress to Emerson. All of these factors contributed to a higher gas balance in the WCSB, putting downward pressure on the price of gas at NIT.

Beginning in October 2013, with market participants adapting to the RH-003-2011 Decision and increased FT contracting, the NIT price began to rise and differentials tightened. TransCanada submitted that while NIT may have been disconnected for a brief period in the summer of 2013, CAPP and its members have benefited from the narrowing of the differential since then.

TransCanada submitted that pricing discretion remains in effect today, as it did last summer, yet basis differentials between NIT and other locations have narrowed significantly. This occurred notwithstanding the fact that the bid floors posted by TransCanada for discretionary services were not materially different from those posted last summer. In contrast, market conditions had changed. First, Alberta storage balances at the end of June 2014 were 35 per cent below the ten year average. Second, WCSB export facility capabilities have been restored after the floods of last summer. Third, Northern Border had not required a further maintenance outage. Fourth, the market has become accustomed to the elimination of RAM. TransCanada argued that based on these facts alone, it would be impossible to conclude that pricing discretion caused the disconnect at NIT in the summer of 2013 or even contributed to the natural gas price effects upstream or downstream of the Mainline.

Dr. Carpenter expressed concern that in describing the summer 2013 netback effect, Dr. Orans focused his observations on the Empress to Emerson spot price spread. Dr. Carpenter argued that Emerson is not a very liquid delivery point and therefore the reported spot price at Emerson can be influenced by many factors. Moreover, Dr. Orans' emphasis on spot price spreads was misplaced, because spot prices are not forward-looking. Dr. Carpenter stated that if pricing discretion was expected to have a sustained effect on netback prices, then one would expect that the implementation of pricing discretion would have been accompanied by a sharp and sustained increase in the forward spread, of which there was no indication.

TransCanada submitted that its use of pricing discretion did not impact downstream commodity prices. TransCanada argued that price spikes during the winter 2013-2014 were not limited to Mainline points and in fact, price spikes experienced in Mainline market areas were highly correlated with price spikes realized in other markets further removed from the Mainline.

Moreover, the winter of 2013-2014 was one of the coldest on record in the past 35 years. As a result, prices were higher than previously experienced.

TransCanada argued that Dr. Cicchetti's hypothesis that 'higher IT bid floor prices on the Mainline would cause commodity prices to increase at inter-connected hubs' is not a reasonable hypothesis and is not supported by any evidence. A better hypothesis would have been that TransCanada's IT pricing behaviour was not determining the market, but was following the market.

Dr. Carpenter submitted that Dr. Cicchetti's regression analysis suffered from a number of flaws, specifically: the choice of pricing locations, the regression specifications (explanatory variables), and autocorrelation problems. Dr. Carpenter submitted that a correction to account for the autocorrelation problem alone would change Dr. Cicchetti's regression results, such that his conclusions can fairly be described as spurious and unreliable.

Dr. Carpenter submitted his own regression results, which replicated Dr. Cicchetti's original regressions and corrected for the autocorrelations. Dr. Carpenter submitted that his results demonstrated the r-squared statistic to be significantly lower than that reported in Dr. Cicchetti's original results. Instead of explaining approximately 80 per cent of the variation in prices, these results indicate that the corrected equations explain typically less than 25 per cent of the variation in the changes in prices, and in some cases there is little-to-no explanatory power. Dr. Carpenter stated that the low explanatory power indicates that there are likely other important variables that were omitted from Dr. Cicchetti's equations and should have been included. Dr. Carpenter emphasized that if TransCanada's bid floor prices were correlated with the market conditions that TransCanada is reacting to in determining its bid floors, then in the absence of variables which attempt to capture prevailing market conditions, the bid floor prices may simply be acting as a proxy for market conditions in these equations.

TransCanada submitted that in looking at comparisons of daily natural gas prices and IT bid floor prices submitted by Dr. Cicchetti, one can see that on some dates IT bid floors and commodity prices move in the same direction and to similar levels, but there are also numerous instances where the IT bid floors and commodity prices do not move in the same direction or near to the same levels. TransCanada argued that all that the Board can conclude from this analysis is that the market experienced a lot of volatility during this time period.

With respect to Dr. Orans' assertions that TransCanada's aggressive pricing behaviour contributed to the extreme prices in eastern markets, Dr. Carpenter observed that Dr. Orans failed to appreciate the kind of day-to-day frictions that occur in markets; that TransCanada established its bid floors in advance and in anticipation of uncertain market outcomes; and that bid-ask spreads were to be expected, particularly where markets were volatile.

Under cross examination, Dr. Carpenter confirmed that bid floor levels are one of many factors that influence spot basis differentials. Dr. Carpenter summarized that even if pricing discretion were to affect downstream prices for short periods of time, if the price effects cannot be sustained, there was no effect on economic efficiency, the reasonableness of tolls, or the public interest. Dr. Carpenter added that under competition law theory, the concept of 'sustained' applied to a non-transitory period of time, which is typically referred to as longer than one year.

Mr. Reed submitted that it is possible that STFT and IT bid floors influence commodity prices, but there was no evidence submitted by intervenors that pricing discretion had influenced commodity prices. Mr. Reed further submitted that TransCanada is under a must-offer status, such that if capacity is available, TransCanada must offer this capacity. If TransCanada's bid floors are constrained, the price level acts as a cap on the transportation price for discretionary services and can depress the price other parties will receive in the secondary market. In Mr. Reed's view, this does not necessarily, and probably would not, affect the price of gas at the destination market. However, it would affect who gets the economic rent resulting from such a transaction.

Overall, TransCanada submitted it had gained and continues to gain experience using pricing discretion, and that neither the Board nor TransCanada can expect the past year to be indicative of the operation or effects of TransCanada's pricing discretion over the term of the application. TransCanada characterized the period since the implementation of pricing discretion as a transition period and emphasized that pricing discretion occurred during a period of extreme weather.

TransCanada stated that its use of pricing discretion is to the benefit of all Mainline shippers, and is consistent with the public interest and applicable tolling principles.

TransCanada argued that CAPP's and Centra's opposition to pricing discretion was based on fundamental disagreement with the Board's conclusion in the RH-003-2011 Decision that costs should be recovered from those that use the pipeline. TransCanada argued that Centra's position, at its core, is that a shipper with firm contracting needs should be able to contract for several months of STFT service that over the term costs less than annual FT.

Mr. Reed submitted that TransCanada's express objective in seeking pricing discretion for discretionary services in the RH-003-2011 proceeding was to optimize revenues from all Mainline services, and the Board both recognized and supported this objective by providing TransCanada with pricing discretion notwithstanding the express acknowledgment that tolls for discretionary services may be very high at certain times.

Mr. Reed submitted that while predictability and stability are important considerations for FT tolls, they are not an important or required objective for the pricing of discretionary services, because a shipper wanting tolling stability and predictability can contract for FT.

TransCanada argued that the continuation of pricing discretion is warranted in light of the risks that TransCanada will assume under the application.

TransCanada argued that reduction in risk is explicitly accounted for in the application. The reduced risk is reflected in the reduction of ROE from the current 11.5 per cent to 10.1 per cent.

TransCanada submitted that intervenor proposals to limit pricing discretion should be rejected.

TransCanada stated that the discretionary pricing model that CAPP proposed does not encourage shippers who require firm service to contract for annual firm capacity. Shippers that require guaranteed service would be made aware of the IT and STFT maximum bid floors in advance of the gas year. Knowing that those bid floors could not be increased but could be decreased provides shippers the luxury of waiting to contract as long as possible.

TransCanada submitted that Dr. Orans' suggestion that the auction mechanism will result in prices above the bid floor more frequently than it has is unrealistic and misguided. First, TransCanada argued that having caps on pricing discretion would, under certain circumstances, limit it from setting bid floors close to the market value. Second, the auction mechanism would not result in prices above the bid floor more frequently than under the current environment. With current pricing discretion, shippers are uncertain of what future prices will be and are therefore more likely to increase bid floors to secure capacity. Under the CAPP proposal, shippers have certainty as to what the future bid floors will be and will likely be unwilling to bid up prices on any given day. Third, setting bid floor levels by the 15th of February of the previous gas year will impede TransCanada's opportunity to capture market opportunities.

Mr. Reed testified that CAPP's and Centra's proposed limits on TransCanada's pricing discretion must be considered in the context of the benefits pricing discretion has achieved. The existing pricing flexibility allowed TransCanada to capture a portion of the economic rent that exists from time to time, for the benefit of all Mainline shippers, instead of that rent being captured by individual parties.

Dr. Carpenter submitted that CAPP's proposal serves to limit TransCanada's ability to effectively compete in the secondary market to the benefit of other, unregulated secondary market participants. Dr. Carpenter stated that TransCanada, while subject to regulated FT tolls, does not have market power with respect to discretionary services and should thus be on an equal footing with competitors in respect of those services.

TransCanada submitted that the CAPP proposal gives shippers a free option to use the system when they want. TransCanada emphasized that such contracting behaviour was the reason that the Mainline got into the situation that led to RH-003-2011. TransCanada also argued that CAPP's proposed model disregards the Board's objective for pricing discretion that economic rents available from market opportunities should be shared.

Overall, TransCanada expressed that objections of those opposed to the continuation of unlimited pricing discretion can be viewed as a natural reaction of a party experiencing a reduction in its share of the economic rent that arises when market prices increase. Pricing discretion allowed TransCanada to now capture some of that economic rent, instead of that rent being captured by marketers, producers or other parties that previously benefited from TransCanada's inability to respond to market conditions.

TransCanada also emphasized that it did not agree with Centra's position that pricing discretion is unregulated. TransCanada submitted that the Board has a complaints process, and that if a party is concerned about the way pricing discretion is being exercised, that party can come to the Board and file a complaint. TransCanada submitted that despite the positions of some parties on the continuation of pricing discretion, no one filed a complaint about pricing discretion.

TransCanada also disagreed with CAPP's position that TransCanada acts as a traffic cop and directs gas to TransCanada's affiliates. TransCanada submitted that there was no evidence on the record that TransCanada's pricing of discretionary services had done anything other than attempt to maximize revenues by capturing the market opportunities available to it. There was also no evidence that TransCanada's pricing discretion was aimed at directing gas to its affiliated companies.

In response to parties who relied on Views of the Board in RH-003-2011 regarding pricing discretion, specifically that "it is unlikely there will be many days when TransCanada will be able to achieve pricing for IT and STFT service over a pricing level of 300 per cent of the FT toll," TransCanada submitted that the Board discussed achieving the bid floor level, not setting that level.

4.1.1 Views of the Board

Since the implementation of the RH-003-2011 Decision on 1 July 2013, TransCanada's exercise of pricing discretion resulted in significantly increased FT contracting and higher-than-forecast net revenues. In September 2014, the TSA balance, net of incentive payments, was forecast to total $440 million at the end of 2014 and the LTAA was

forecast to be positive in 2015, due to the proposed transfer of the TSA balance to the LTAA. The RH-003-2011 Compliance Filing of May 2013 had forecast the LTAA balance to be significantly negative at this time. The turnaround in Mainline revenues in a period of slightly over one year is largely attributable to the implementation of pricing discretion for short-term services, which incented shippers to reverse the contracting patterns prior to RH-003-2011 and instead contract for FT services to meet firm needs.

TransCanada requested that pricing discretion continue until 2020 to prevent prior contracting behaviour from returning. Although firm contracts for the next two years are very close to TransCanada's forecast billing determinants, there continues to be a shortage of FT contracts from 2017 onwards. The Board is of the view that capping pricing discretion will increase the likelihood of lower FT contracting for 2017 onwards because shippers will resort to using discretionary services to meet firm needs, particularly on paths where there is excess capacity. The Board continues to be of the view that shippers with firm needs should pay the annual costs of Mainline capacity and that pricing discretion will continue to induce shippers with firm needs to contract for FT services. Moreover, pricing discretion is likely to result in higher net revenues than if pricing discretion were capped.

The Board has heard extensive evidence on whether pricing discretion affected commodity prices following the implementation of the RH-003-2011 Decision. The Board notes that pricing discretion has been described as unique and unprecedented by all parties, and that the degree of success of pricing discretion was not anticipated by anyone, including TransCanada and MAS. On 1 July 2013, the market was faced with a new set of Mainline services: lower priced fixed FT tolls, volatile IT and STFT bid floors and the elimination of RAM. The Board would anticipate that naturally, a period of transition would occur immediately after the implementation of the RH-003-2011 Decision. While differentials between NIT and other hubs increased during the early period of pricing discretion, they decreased shortly thereafter and have remained below historical levels.

The Board heard extensively that there are many factors that impact commodity prices, and that TransCanada's bid floors are only one such factor. Evidence indicated that on certain occasions, IT bid floors and commodity prices were strongly related, while on other dates, there was little to no relation. The Board reviewed all the statistical analysis evidence submitted, including the regression analysis submitted by Centra with respect to TransCanada's setting of bid floors and its effect on commodity pricing. The Board is of the view that the regressions submitted had poor explanatory power due to issues associated with autocorrelation, a poor weather variable chosen and missing explanatory variables. The North American market is highly integrated, and there are other factors that could explain why prices at Emerson and at other hubs increased. The Board agrees with TransCanada that capped levels of pricing discretion, particularly with bid floors known well in advance, will increase the likelihood that bid floor prices will impact commodity prices, because pricing patterns would be fully predictable.

The Board notes that the first year of pricing discretion coincided with one of the coldest winters in 35 years, when below average temperatures significantly increased demand and rapidly depleted storage levels, particularly in eastern Canada. Combined with

regional pipeline bottlenecks, this in itself is sufficient to result in higher natural gas commodity prices.

Overall, the Board continues to believe that shippers can mitigate their exposure to volatile IT and STFT services by purchasing FT. On paths where FT is not available, shippers can request additional capacity from TransCanada. The Board agrees with TransCanada that shippers with firm requirements should not rely on the availability of IT to meet their firm requirements, and that shippers need to plan ahead to meet incremental firm service requirements.

The Board has heard that 70 per cent of TransCanada's bid floors were not purchased, but that the market met its needs nonetheless. However, the Board has also heard that in some circumstances, particularly during periods of high demand, natural gas is not offered for sale until TransCanada's bid floor prices are released and bid floor prices are subsequently incorporated into commodity prices at downstream hubs. The Board finds this to be rational behaviour for marketers and other market participants who want as much information as possible in order to assess the value of their capacity at that time. If bid floors are higher than the market is willing to bear, transactions will not occur. Nevertheless, the Board notes that while such circumstances are transitory, the Board is concerned that during these periods, the market may view TransCanada, the operator of the pipeline, as being in possession of information that may not be available to other market participants. This may include shipper's specific nomination volumes and detailed diversion volumes. Therefore, parties competing with TransCanada may rely more on TransCanada's bid floors in pricing their capacity. The Board is of the view that in such circumstances, when compared to other periods, TransCanada's posted bid floors are more likely to impact commodity prices than other market factors. The Board has further addressed this issue in Section 4.2.

The Board is of the view that the exercise of pricing discretion will evolve with the market for Mainline capacity. At the close of the evidentiary record, TransCanada has had 14 months of experience in setting bid floors on the Mainline. During this period, FT contracts increased from 3 PJs to almost 7 PJs. Moreover, implementation of pricing discretion occurred during one of the coldest winters in 35 years. However, while first quarter 2014 DMR was high at $384 million, second quarter 2014 DMR was significantly lower, at only $4 million. The Board agrees that high levels of DMR generated in the first twelve months are unlikely to be representative of DMR in the future.

As of mid-September 2014, contracted FT volumes for the next two years are close to TransCanada's forecast of billing determinants. The Board is of the view that the Mainline's contracting profile is significantly different compared to when pricing discretion was first implemented and this presents TransCanada with a new paradigm for pricing discretion. TransCanada's exercise of pricing discretion will require heightened considerations and a careful balance in encouraging FT while at the same time capturing discretionary opportunities.

The Board is of the view that there are significant opportunities for the Mainline to compete with other pipelines from the WCSB in delivering gas to markets. However, the Board notes that the proposed tolls are higher than what the Board determined to be the upper limit of competitive tolls in the RH-003-2011 Decision. Furthermore, the NIT

differential with Henry Hub (and other hubs) is below its historical level. The Board heard that current FT tolls on the Mainline, as well as IT tolls, are not always economic. To attract incremental revenues, TransCanada's pricing desk will have to effectively use its discretion in promoting the use of the pipeline, including the discount of IT to below FT levels.

Overall, it is the Board's view that multi-year fixed tolls and the net revenue incentive mechanism implemented in this decision continue to provide TransCanada with strong incentives to make appropriate decisions in how it sets IT and STFT bid floors. Material misjudgments in the use of pricing discretion will result in higher deferral account balances, leading to higher tolls and a potential return to the situation that existed prior to the implementation of the RH-003-2011 Decision.

Decision

The Board decided to maintain pricing discretion as was established in the RH-003-2011 Decision. As discussed in Chapter 8, the Board will review the continued appropriateness of the existing pricing discretion for the 2018 to 2020 time period in a future TransCanada Mainline tolls application.

4.2 Transparency and management of pricing for discretionary services

Views of TransCanada

TransCanada submitted that in addition to publicly available information, from time-to-time its pricing desk employees access historical information on nominated quantities and cleared bid prices in setting bid floors. This historical information complements publicly available information on scheduled deliveries at each Mainline receipt and delivery location. TransCanada added that individuals working at the pricing desk are employees of the regulated Mainline and therefore have access to the same level of information as any other employee. TransCanada submitted that this includes access to information on individual shippers' nominations and that this information is also non-public.

Views of the Participants

BP

BP submitted it remains concerned about the transparency of how TransCanada offers and prices its discretionary services and the ongoing need for better information in that regard. BP also submitted that the use of shipper-specific proprietary information that TransCanada has by virtue of its role as operator of the Mainline needs to be addressed. Specifically, BP argued that a firewall, or some other similar mechanism, needs to be implemented to prevent employees on TransCanada's pricing desk from having access to non-public, shipper-specific information.

CAPP

CAPP recommended that the Board require TransCanada to increase reporting for discretionary services pricing on the Mainline. CAPP submitted that as long as TransCanada retained some flexibility in its discretionary services offerings, TransCanada should publish a summary report

of its short-term capacity offerings and their results. For IT services, the summary report should contain the following information, submitted on a path-by-path basis:

- daily bid floors for IT;
- daily clearing prices for IT;
- daily basis spreads for key paths;
- indication of the frequency that the IT bid floor exceeded the spread;
- indication of the frequency that the IT clearing price exceeded the spread;
- daily volume of IT offered;
- daily volume of IT transported.

For STFT, CAPP recommended a report that contains the results of any STFT offerings, bid floors, clearing prices, and total volumes transported on a path-by-path basis.

Dr. Orans submitted that this additional reporting would provide clarity to the market on TransCanada's pricing practices and the Board with increased transparency for monitoring and evaluating TransCanada's practices. This would help to inform future regulatory decisions within the context of TransCanada's past activities. Under cross-examination, Dr. Orans stated that in granting pricing discretion to TransCanada, the Board had assumed the existence of a competitive secondary market, and therefore the Board has an obligation to ensure markets are competitive.

Overall, CAPP submitted that TransCanada's pricing desk has access to detailed shipper information and has been aggressively competing with shippers. CAPP's proposal for greater transparency is intended to make the field level for all participants in the marketplace.

In response to TransCanada's position that a consultation with shippers should first occur before it can be determined whether changes to the current reporting are warranted, CAPP submitted that previous consultations on this matter were frustrating and uneventful. CAPP therefore emphasized the Board should provide guidelines for reporting requirements and identify the pillars it was seeking to ensure reporting requirements are reasonable.

Centra

Centra submitted that any information disclosure that brings greater transparency to the market would be a step in the right direction. Centra agreed with CAPP's position that the Board should provide guidelines and identify pillars it is looking for to ensure reporting requirements are reasonable.

Centra submitted that TransCanada's pricing desk employees have access to transactions between shippers, and shipper-specific nomination information, including volumes and transportation paths, current or historic. This may also include access to shipper-specific, non-public information on regulated TransCanada affiliates. Centra argued that such access provides TransCanada with information and market intelligence that is not available to any other market participant competing against TransCanada in the secondary transportation and commodity market.

Centra witness Mr. Sanderson submitted that based on his review of TransCanada's Code of Conduct, there are no restrictions on TransCanada's pricing desk employees accessing non-public information. The current Code of Conduct is therefore insufficient, as it enables TransCanada to have asymmetric access to information regarding the wider natural gas market. Centra therefore argued that the Board should impose a prohibition on TransCanada's access to and use of any and all non-public shipper-specific information in the course of exercising its pricing discretion, and that TransCanada should report on any breaches that occur.

IGUA

IGUA submitted that United States Federal Energy Regulatory Commission (FERC) collects transaction data, including secondary market transactions, from all market participants in the United States energy market with the objective of increasing transparency. IGUA submitted it supported efforts of the Board to achieve greater transparency in natural gas markets through the posting of additional information, particularly available capacity from TransCanada and from shippers.

TransCanada Reply

TransCanada stated that CAPP's data reporting proposals are unjustified and unnecessary.

TransCanada opposed CAPP's request that it be directed to provide additional information to enhance transparency in relation to discretionary services pricing. TransCanada argued that the additional information sought by CAPP is either already provided by TransCanada and/or is available from third party sources. Any additional information is unnecessary and will serve to undermine the effectiveness of pricing discretion and disadvantage TransCanada in competing in the secondary market. TransCanada stated that that there exists today considerable transparency from the Mainline and this exceeds any information available from TransCanada's secondary market competitors, who themselves have information about over-the-counter transactions that is not available to TransCanada.

TransCanada emphasized that a consultation process should first occur before determining whether any change to the current reporting is warranted, and before any change to quarterly reporting requirements is contemplated by the Board. Mr. Schultz suggested TransCanada be allowed to go back to the stakeholder group and discuss what has and has not worked, what additional information would be of value, and whether or not there is any other information that has not been contemplated that would be useful for reporting purposes.

Regarding pricing desk employees' access to non-public information, TransCanada disagreed with Centra's position that because TransCanada's pricing desk has access to shipper-specific and non-public information that some form of restrictions should be imposed. TransCanada submitted that the Mainline had always used the information it had regarding its customers and its operations to market Mainline capacity. Restricting access of the pricing desk to customer information would make it impossible for the pricing desk to work towards the Board's objective of TransCanada using pricing discretion for maximizing overall revenues.

Nonetheless, TransCanada submitted that if the Board had any inclination to consider limitation of access of the Mainline pricing desk to information for its use in setting prices for discretionary

capacity, this should only be done after a comprehensive review of the information available to, and limitations on all secondary market participants in the setting of prices for pipeline capacity.

4.2.1 Views of the Board

The Board understands that various Mainline stakeholders have concerns about TransCanada's internal management of access to shippers' non-public information for its pricing desk employees as well as the reporting of information on the sale of short-term services and transparency of information regarding the secondary market.

The Board notes that throughout its evidence and during cross examination, TransCanada emphasized it is competing with the secondary market. Several intervenors expressed the view that TransCanada's pricing desk should not have access to non-public information as this creates asymmetry between parties competing in the sale of short-term capacity on the Mainline.

In responding to Undertaking 4, TransCanada submitted that employees of its pricing desk have access to non-public information, including path-specific shippers' nominations. The Board notes that TransCanada witnesses submitted that they did not know to what extent such information was used in setting bid floors for IT and STFT. TransCanada did not provide any evidence which would support that restricting access of the pricing desk to customer information would make it impossible for the pricing desk to work towards maximizing overall revenues.

During the oral hearing, TransCanada submitted that its pricing desk employees have access to non-public information, including path-specific shippers' nominations. The Board is concerned that access to non-public information available to TransCanada's pricing desk employees could be construed to offer an unfair advantage to TransCanada over secondary market participants.

The Board is of the view that TransCanada should not be advantaged on the account of its role as operator of the Mainline with access to non-public information. TransCanada and secondary market participants compete in the market for the sale of short-term capacity, and should generally be competing on a level playing field in order for the secondary market to operate as a check on the exercise of pricing discretion.

As a first step the Board directs TransCanada to initiate a comprehensive review of the specific non-public information that TransCanada's pricing desk has access to, including non-public information on TransCanada's affiliates, and how this information could, in theory and practice, influence the setting bid floors for IT and STFT. The Board is primarily concerned about access of pricing desk employees to shippers' transactions, including volumes and transportation paths, real time and historic.

TransCanada is directed to provide remedies on how it will prevent access to and use of non-public information in the setting of bid floors for discretionary services. Potential remedies may include the implementation of firewalls between the pricing desk and the regulated Mainline entity, inclusive of communications and access to information; a separate code of ethics for pricing desk employees; and/or an update to the Mainline's Code of Conduct, amongst others. Given the concerns expressed by participants in this

proceeding, the Board is of the view that TransCanada's review will benefit from consulting with Mainline stakeholders on this matter.

TransCanada is directed to provide the results of its internal review and consultations with stakeholders to the Board by 31 March 2015.

Related to information management and transparency, the Board notes that while TransCanada already files information on IT and STFT bid floors with the Board on a quarterly basis, parties here have expressed that additional and more frequent posting of information may be required.

In this proceeding, parties submitted that the Board should direct TransCanada to post daily, by path, cleared bid floors for IT and STFT and daily volumes of IT and STFT transported on the Mainline. Participants submitted that increased reporting requirements are intended to increase competition between TransCanada and the secondary market in the sale of short-term Mainline capacity. Parties requested guidance from the Board on what information needs to be reported to ensure that reporting requirements are reasonable.

The Board notes that under current reporting requirements, cleared bid floors for IT and STFT are not posted and only TransCanada's employees have access to cleared bid floor prices, as discussed above. Shippers that participate in the secondary market (for either short-term capacity releases or bundled transportation and commodity deliveries) have information on transactions that is not available to TransCanada. The Board has also heard that parties who wish to purchase capacity (or bundled transportation capacity and commodity) from the secondary market do not always have information on whether such capacity is available and who is willing to offer it.

The Board is of the view that, in general, reporting requirements should not disadvantage any party in competing with others for the sale of short-term capacity and that reporting of any information should be symmetrical between TransCanada and Mainline shippers. The Board is of the view that limiting access of pricing desk employees to non-public proprietary information within TransCanada may decrease the necessity for additional reporting. The Board makes the general comment that it acknowledges the potential for information asymmetry if enhanced reporting requirements for TransCanada are implemented and suggests that, if pursued, they should be accompanied by enhanced reporting requirements of other secondary market participants. The Board is of the view that secondary market information, including available capacity, may be opaque and therefore encourages TransCanada and shippers to arrive at ways to increase transparency on where capacity in the secondary market may be available. To be clear, at this time the Board is not proposing that it begin regulating the reporting requirements of other secondary market participants.

TransCanada is already under the direction of the Board to consult with shippers on the content of its Quarterly Surveillance Reports and whether any amendments need to be made to reporting requirements, a direction which flows from the Board's response to TransCanada's Compliance Filing under RH-003-2011 in June 2013 and for which TransCanada was recently granted a time extension. The Board in this proceeding has directed TransCanada to review and consult on its internal management of non-public information as it relates to its exercise of pricing discretion. The Board anticipates that

TransCanada will take advantage of the connections between these issues and the consultation on reporting requirements and engage its stakeholders on both.

In addition to participating in the aforementioned consultations, the Board further invites interested parties to review TransCanada's 31 March 2015 submission and submit their comments to the Board by 30 April 2015. Upon receipt of submissions from interested parties, the Board may hold a written process or a technical conference to determine measures to address the transparency and management of discretionary services issues.

Decision

The Board directs TransCanada to provide remedies on how TransCanada will prevent access to and use of non-public, shipper-specific information in the setting of bid floors for discretionary services.

Chapter 5

Revenue requirement

5.1 Revenue requirement and rate base

Views of TransCanada

TransCanada applied for a revenue requirement for each year between 1 January 2015 and 31 December 2020. These proposed revenue requirements were used to establish tolls for each respective year. TransCanada stated that the revenue requirements, as well as the associated rate bases, were determined in a manner consistent with the 2013–2017 Compliance Filing components established in the Board's RH-003-2011 Decision, with an extended time period to 2020. The elements of the revenue requirement include return and income tax, the TransCanada Contribution, the Annual Bridging Amount (ABA), and the cost of service components.

TransCanada stated that the proposed rate bases are consistent with the Compliance Filing, with two changes:

- The net plant balances have been updated based on a more current forecast, which includes the new capacity capital projects.
- Adjustment account balances differ due to elimination of the $95 million LTAA contribution for 2015 to 2017 and inclusion of the Bridging Amortization Account (BAA).

The rate bases for the period 1 January 2015 to 31 December 2020 include the following major capital additions to the Eastern Triangle:

- Hamilton Line – $25 million (November 2015 In-Service)
- King's North Connection Pipeline Project – $126 million[2] (November 2015 In-Service)
- 2016 Mainline Expansion – $240 million (November 2016 In-Service)

The BAA is included in the Mainline rate base to capture the forecast annual variances associated with establishing fixed tolls during the period 1 January 2015 to 31 December 2020 and to amortize the Bridging Contribution for Eastern Triangle short-haul service over the period 1 January 2015 to 31 December 2030. The bridging adjustment refers to the fixed annual amount placed in the BAA and included in rate base to account for variances associated with build-up and recovery of the Bridging Contribution and the forecast annual variances associated with establishing fixed tolls during the fixed-toll period. The Bridging Adjustment is included in the BAA and carried in the rate base; amounts added to or amortized from the BAA function in the same manner as adjustments to the LTAA. As the balance of the BAA will be amortized over the period 1 January 2015 to 31 December 2030, the account will not be required after 31 December 2030.

[2] TransCanada submitted that this cost is expected to increase by approximately $100 million, primarily due to higher land costs.

The revenue requirement impact resulting from balances in the BAA are reported together in the revenue requirement as the ABA. The ABA is the amount to be included in the revenue requirement each year between 2015 and 2020 for that year's Bridging Contribution[3], including associated income tax and return. The ABA consists of two adjustments, one to account for the period to recover the Bridging Contribution and the other to account for variances associated with charging fixed tolls. The ABA associated with the Bridging Contribution aligns with the Bridging Contribution received by shippers and amortized (until 2030 for eastern short-haul shippers, and until 2020 for all other shippers, including eastern long-haul shippers). The ABA associated with fixed tolls relates to the over- or under-collection of revenue as a result of charging fixed average tolls for 2015 to 2020. As a result there will be no effect from the ABA on the LTAA.

The proposed gross revenue requirement assumptions for 2015 to 2020, and any differences from the Compliance Filing, are listed below. Service component costs were updated based on the most recent forecasts and included in the application.

- TBO costs includes a new TBO contract with Enbridge.
- Storage operating costs, NEB cost recovery, Regulatory proceeding costs and collaborative costs and Operations, Maintenance and Administrative (OM&A) costs are planned to increase by an inflation rate of 2.0 per cent per year.
- Pipeline integrity costs are held constant at $100 million per year.
- The depreciation and amortization rates used for calculation of depreciation expense and amortization of the LTAA for 2015 to 2020 are based on the average composite depreciation rates approved in the RH-003-2011 Decision.
- The return on rate base is calculated based on a ROE of 10.1 per cent on a 40 per cent deemed common equity and a forecast of debt cost.
- Income taxes for 2015 to 2020 are calculated based on assumptions that are generally consistent with those approved in the RH-003-2011 Decision including an income tax rate of 25.937 per cent. Timing differences are either consistent with the RH-003-2011 Decision or have been updated based on related assumptions of rate base, depreciation and debt. The capital cost allowance for each year is the amount approved in the RH-003-2011 Decision plus an amount calculated for additional capacity capital expected to be spent in those years.
- Municipal and provincial capital taxes are consistent with the Compliance Filing with a forecast for additional taxes due to additional capacity capital assumed in the application. These taxes are forecast to increase by 3.0 per cent per year.
- Electric costs and tax on fuel are lowered in the application relative to the Compliance Filing due to a more recent forecast for 2015 and then increased by the general inflation rate of 2.0 per cent per year for the period 2016 to 2020.

[3] The Bridging Contribution is defined as the revenue shortfall allocated to the Eastern Triangle, Prairies and NOL segments after adjusting the Eastern Triangle short-haul tolls to recover costs of the Eastern Triangle and applying Compliance Tolls for the remaining paths.

- TransCanada Contribution of $27 million (pre-tax), $20 million (after-tax) annually is included.
- Addition of the ABA in the revenue requirement.

The application also details the basis for calculating allowance for funds used during construction and inclusion in the revenue requirement of costs and expenses reasonably and prudently incurred by TransCanada as a result of its TBO contracts on the TQM, Union, Enbridge, and the GLGT Systems. The application does not preclude any other initiative by TransCanada designed to reduce the Mainline's cost of service between 2015 and 2030.

In response to a Board request during the oral portion of the hearing, TransCanada submitted an illustrative update of the revenue requirement based on current information. The cost assumptions included changes resulting from:

- Forecast year-end 2014 TSA balance applied to LTAA.
- Change to costs associated with King's North Connection Pipeline Project.
- Change to costs including TBO, pipeline integrity and insurance deductible costs, electric costs and tax on fuel, OM&A and greenhouse gas emissions costs.
- Change to storage working gas.

These assumptions have an impact on various line items in the rate bases and revenue requirements including the ABA.

TransCanada submitted that the cumulative impact of the changes to these cost assumptions on the revenue requirement total a difference of $8.0 million over the 2015 to 2020 period. However, on a segmented basis, the cost increase was higher in the Eastern Triangle, which is subsequently slightly offset by an overall lower Bridging Contribution and associated lower amortization of the Bridging Contribution for Eastern Triangle shippers out to the end of 2030.

TransCanada submitted that the revenue components included in the application, both firm contract levels as well as the DMR forecast, remain appropriate. TransCanada concluded that the tolls originally filed in the application remain reasonable and should be approved by the Board. The differences that would result from the updated information are *de minimus* and should be dealt with through the LTAA mechanism as originally intended in the application.

Views of Participants

ANE

In ANE's view, there are two cost elements in TransCanada's proposed revenue requirement that appear overstated. The first is pipeline integrity and insurance deductible costs of $100 million each year. ANE observed that TransCanada's actual pipeline integrity costs have been substantially below this level, due in part to expense reductions that result from the Energy East project paying a portion of the costs. ANE observed that TransCanada also indicates that pipeline integrity costs were not updated as part of the new revenue requirement forecast used for the proposed revenue requirements.

The second element that ANE suggested requires an adjustment is electric costs and tax on fuel. The monthly expense for the second half of 2013 and the quarterly expense for the first quarter of 2014 appear to be considerably lower than the level incorporated by TransCanada in its proposed revenue requirements. ANE suggested that changing flows on the Mainline may be contributing to reductions in this category of expense. ANE recommended a reduction of electric costs and tax on fuel to a level equivalent to the actual expense for July 2013 through June 2014. Regardless of whether the Board maintains the Compliance Tolls or implements aspects of this application, ANE recommended that pipeline integrity and insurance deductible costs, electric costs and tax on fuel be set at levels consistent with TransCanada's 2013 experience.

Centra

Centra proposed that if the application is largely approved, a more appropriate approach to ROE would be to differentiate ROE by Mainline segment effective 1 January 2015, and for TransCanada to be subject to an earnings moratorium on the Prairies Line and NOL for the 2015 to 2020 timeframe, with these dollars being used to accelerate the depreciation of the Prairies Line.

IGUA

IGUA indicated that since it does not object to the settlement as a package, it has no objection with respect to the appropriateness of the revenue requirements and rate bases over the 2015 to 2020 term.

TransCanada's Reply

In TransCanada's view, ANE's evidence focused on certain individual components of the revenue requirements, while ignoring other components, and thus fails to consider the overall aggregate level of the revenue requirements utilized to derive tolls for the 2015 to 2020 period. TransCanada stated that there are components of the revenue requirements that will be higher than the costs included in the application and TransCanada will be challenged to manage the aggregate costs to the levels reflected in the application forecast. TransCanada submitted that on balance, the forecast of Mainline costs reflected in the derivation of the proposed tolls is reasonable such that there is no basis for any downward adjustments.

TransCanada suggested that Centra's recommendation for an earnings moratorium on the Western Mainline over the 2015 to 2020 period, used to accelerate depreciation of the Prairies Line, is an approach contrary to the requirements of the fair return standard and Board precedent and policy, and is not warranted in the current circumstances of the Mainline.

5.1.1 Views of the Board

The Board finds that, on balance, the proposed revenue requirements for 2015 to 2020, including the return and income tax, TransCanada Contribution, ABA and cost of service elements are reasonable. The Board also finds reasonable the proposed rate base components for 2015 to 2020, including the adjustment accounts – the LTAA and the BAA – and the Capacity Capital Additions allocated to the Eastern Triangle rate base.

The Board does not accept Centra's proposal to differentiate ROE by Mainline segment effective 1 January 2015, and for TransCanada to be subject to an earnings moratorium on the Prairies Line and NOL for the 2015 to 2020 timeframe, with these dollars being used to accelerate the depreciation of the Prairies Line. The Board considers the review of depreciation rates premature and unsupported by evidence at this time, and the consideration of an earnings moratorium on two Mainline segments without merit.

Decision

The Board approves the proposed revenue requirements and rate bases for the 2015 to 2020 period.

5.2 Treatment of the TSA and LTAA

Views of TransCanada

TransCanada submitted that one factor that led to the Settlement was the potential early re-visitation of Mainline tolls pursuant to one or more of the off-ramps in the RH-003-2011 Decision that can be triggered by the level of the balance in the TSA or the repurposing of Mainline assets. TransCanada stated that the TSA reached a positive balance at the end of 2013. The TSA was established in the RH-003-2011 Decision to capture the cumulative annual differences between actual total revenues and actual total costs (net of any payments under the incentive mechanism) in order to maintain multi-year fixed tolls.

While the application assumed a TSA balance of zero at the end of 2014, subsequent information presented in the proceeding predicted a positive balance at the end of 2014 of $440.6 million. TransCanada proposed to transfer the TSA balance to the LTAA, thus eliminating the TSA at the end of 2014. TransCanada observed that this transfer to the LTAA would result in a mitigated amount of the LTAA balance transfers to Eastern Triangle tolls post-2020. In TransCanada's view, this proposed approach is consistent with the cost causation principle because the LTAA, representing a system-wide obligation, would be eliminated or virtually eliminated by the TSA, representing a system-wide revenue collection greater than the system-wide revenue requirement.

TransCanada did not support crediting a positive TSA balance at the end of 2014 to the revenue requirement used to derive the 2015 tolls because it would not achieve the application's intended goal of providing toll stability and certainty to shippers. TransCanada observed that shippers will receive the benefit of the positive TSA balance under either treatment; the difference is only the time frame when that benefit is recognized. Regardless of the treatment of the LTAA balance post-2020, TransCanada noted that applying the positive TSA balance at the end of 2014 to the LTAA balance will eliminate the existing LTAA obligation for all shippers going forward.

TransCanada noted that crediting the positive TSA balance only to tolls and not transferring the balance to the LTAA would provide substantial benefit to shippers who may only be on the system in the short-term but leaves long-term shippers and TransCanada with managing the recovery of the LTAA balance for many years. TransCanada suggested that by allocating the TSA to the LTAA, TransCanada is appropriately responding to the Board's direction in the RH-003-2011 Decision to utilize the tools provided to it within the given business environment to reduce risk for the benefit of future shippers and TransCanada.

TransCanada stated that the existing LTAA will continue to be included in the Mainline's rate base. The LTAA is to include the following: the existing LTAA balance as of 31 December 2014; an adjustment to eliminate the existing account balance in the TSA as of 31 December 2014, net of incentive mechanism adjustments; an adjustment to eliminate any and all variances between the actual and forecast revenue requirement and the actual and forecast revenue during the period 1 January 2015 to 31 December 2020, net of incentive mechanism adjustments, in order to provide a greater degree of toll stability and toll certainty from year-to-year for shippers.

During the 2015 to 2020 period, TransCanada proposed that the LTAA be amortized at the annual Mainline composite depreciation rate. After 2020, in accordance with the terms in the Settlement, the LTAA balance is proposed to be included in the Eastern Triangle rate base and amortized at the Eastern Triangle depreciation rate until the balance equals zero.

The application filed in December 2013 showed a negative balance in the LTAA from 2015 to 2020. In subsequent filings, due to the significant positive value of the TSA at the end of 2014 and the proposed adjustment to eliminate the TSA by transferring the balance to the LTAA, TransCanada expected a positive LTAA balance of $4.8 million by 1 January 2015. In TransCanada's view, this reduction of the LTAA balance prior to 2015 is consistent with cost-causation in that it uses a positive deferral account balance derived from past usage to offset a negative deferral account balance that was also derived from past usage. TransCanada suggested that this better achieves intergenerational equity, since it better matches the revenue shortfalls and surpluses to usage from the period in which they were accrued. For toll-making purposes, TransCanada did not propose to update the LTAA balance included in the application.

Views of Participants

ANE

ANE noted that the RH-003-2011 Decision offered two examples of how to treat a positive TSA balance, and both examples, in ANE's view, are reasonable. However, as opposed to TransCanada's proposal, ANE stated that the most important outcome of disposing of the positive TSA balance is that the benefits accrue to shippers. The magnitude of the excess revenues that TransCanada realized under the Compliance Tolls and the incentive payments it will already have retained in 2013 and 2014 has made this outcome even more important. While ANE acknowledged that under the application, the benefit of eliminating the TSA balance would accrue to Eastern Triangle shippers in 2021 or later, ANE noted that there is no basis for delay. As a result, TransCanada's proposal results in the rate base relied upon to establish tolls being over-stated by ten per cent or more for the entire six-year toll period due to this omission, resulting in materially over-stated and unreasonable tolls. This results in a cash flow benefit for TransCanada to the detriment of shippers.

ANE submitted that, as a matter of equity, it is appropriate for shippers to receive the benefit on a comparable timetable as TransCanada. ANE further observed that, given that TransCanada suggests that its application is triggered by the positive TSA balance, the Board should consider the actual TSA balance as of the end of 2014 in adopting revised tolls.

Centra

Centra argued that, if post-2020 segmentation and the proposed allocation of the LTAA is approved in this application, assessment of stranded costs must be made now, as part of the adjudication of the application in the context of the significant abandonment of long-haul contracts by MAS members as contemplated by the Settlement. Centra's position is that allocation of the LTAA should be determined by the Board at the time the 2021 tolls are being adjudicated.

Enbridge and Union

Enbridge and Union submitted that the clear expectation was that the LTAA would be a net liability at the end of 2014 and would likely remain at approximately the same level at the end of 2020. A commitment for the Eastern Triangle shippers to bear the full balance of the LTAA was an attempt to find a compromise that would limit the tolling impact on Prairies and NOL shippers over the transition period.

Enbridge and Union noted that they are cautious about forecasting future balances in the LTAA and explained several factors that could cause significant variations in the LTAA balance by the end of 2020. Accordingly, Enbridge and Union submitted that the TSA should be used to offset the LTAA at the end of 2014 and that the LTAA balance, whether positive or negative, should still be applied to the Eastern Triangle for recovery post-2020.

TransCanada's Reply

TransCanada argued that the recovery of the unamortized Bridging Contribution and the LTAA balance from the Eastern Triangle, as well as the commitment to rolled-in tolling treatment for Eastern Triangle expansions, reflect the balance achieved in resolving the significant uncertainty and tension between TransCanada and its shippers concerning future pipeline expansion and cost recovery in the Eastern Triangle.

TransCanada further submitted that, considering that there are a number of factors that remain uncertain and TransCanada has projected that Western Mainline costs could be reasonably expected to be recoverable post-2020, it is premature for the parties to debate, and for the Board to now determine, whether there will be stranded costs post-2020, let alone responsibility for such potential costs.

5.2.1 Views of the Board

The Board considers the proposed treatment of the LTAA as an adjustment account to eliminate any and all variances between the actual and forecast revenue requirements and the actual and forecast revenues during the 2015 to 2020 period, net of incentive mechanism adjustments, to be reasonable. The Board approves the transfer of the TSA balance as of 31 December 2014 to the LTAA and the subsequent elimination of the TSA. As directed in Chapter 6, TransCanada is to use the actual TSA balance as of 31 December 2014 for this transfer.

Concerning TransCanada's proposal to allocate the LTAA balance to the Eastern Triangle rate base in 2021, the Board has determined that this proposal is appropriate in

the context of the package of gives-and-takes between TransCanada and the settling parties. However, should there be a material change in circumstances when 2021 tolls are determined, the Board may determine that a different allocation of the LTAA is more appropriate.

Decision

The Board approves the proposed treatment of the LTAA and the transfer of the actual TSA balance to the LTAA as of 31 December 2014.

Chapter 6

Toll design

This chapter discusses several toll design related matters, including tolling parameters pertaining to the post-2020 period. Those toll parameters include the amortization of the Bridging Contribution to 2030, rolled-in tolling, and segmentation of the Mainline. The toll parameter dealing with the allocation of the LTAA balance post-2020 was discussed in Chapter 5.

6.1 Maintenance of the Compliance Tolls

Views of TransCanada

TransCanada explained that if the Compliance Tolls were to remain in place, the types of disputes between TransCanada and its shippers that gave rise to the Settlement would likely return. TransCanada concluded that the Compliance Filing revenue forecasts would likely not be reasonable if the Compliance Tolls were maintained.

TransCanada developed three revenue scenarios that could materialize should the Compliance Tolls be maintained for the 2014 to 2017 period but the 2014 and 2015 revenues are updated for recent information. Under each scenario, DMR continues to be estimated at the same level as in the proposed tolls. Two scenarios are based on whether or not MAS members (or some other shippers) file and are successful in a section 71 application to connect their proposed pipeline project of 1,200 TJ/day with the TransCanada Mainline at Maple by November 2016, and were described as reasonable representations of the upper and lower bounds of Mainline revenue. The third scenario assumed that TransCanada builds the three Eastern Triangle capital expansions, the contract billing determinants occur which reflect the changes in contracts associated with the new facilities, and the change in contract quantities and associated revenues from the new facilities is reflected within the change to Mainline firm contract levels. In two of the three scenarios, one where MAS members are successful in a section 71 application and the other where TransCanada builds the facilities, TransCanada achieves less revenue than its revenue requirement by 2017.

TransCanada stated that, while the proposed tolls would be higher than the existing Compliance Tolls and the Board's previous assessment of the upper limit of a competitive toll for the Mainline, a number of factors indicate that they will be competitive. These factors include the results of the recent Mainline open season, the support of MAS, and changed market circumstances. TransCanada observed that these factors are generally applicable to all toll paths on the Mainline. TransCanada discussed the factors influencing whether a particular toll level is competitive for a particular shipper, which included the presence and cost of natural gas alternatives to the Mainline, fuel switching capability and the cost of such alternatives, natural gas market prices, and the degree to which the shipper's demand is firm or can tolerate being interrupted.

Views of Participants

ANE

ANE stated that the RH-003-2011 Decision is fair, results in just and reasonable tolls, and is well reasoned and balanced. Further, ANE stated that the RH-003-2011 Decision established regulatory certainty and stability with respect to Mainline tolls and services, which ANE stated is essential to restoring the Mainline to a position to provide benefits to stakeholders for many years to come. ANE noted that the application is in stark contrast with the Board's recent decisions, and is in contrast to the substantial evidence that indicates that the multi-year fixed toll approach adopted by the Board is working as anticipated. ANE observed that toll levels are important in determining TransCanada's ongoing competitiveness and sustainability.

ANE estimated that between 2015 and 2017, its shippers would pay approximately $100 million dollars more under the proposed tolls relative to the Compliance Tolls, assuming the Compliance Tolls stayed in effect until 31 December 2017. ANE submitted that such a material increase in financial liability would be prejudicial to the ANE shippers. ANE noted this is particularly so in light of the higher return received by TransCanada in the RH-003-2011 Decision, which was intended to compensate TransCanada for the increased business risk it proposes to shift to shippers in the application. ANE also noted that the application is prejudicial to shippers because, by overriding the RH-003-2011 Decision one-third into its term, confidence of the market in the regulatory process is eroded, and shippers are prejudiced when making longer term planning decisions on the TransCanada system.

ANE stated that the application is not warranted on the basis that TransCanada is unable to invest in its system under the RH-003-2011 Decision framework. The proposed changes, including to the revenue requirements, cost allocation methods, and toll design are, in ANE's view, unnecessary to address possible concerns related to investment in expansion facilities. Rather, ANE suggested that the excess revenues from existing services under the RH-003-2011 Decision are more than adequate to offset the capital cost requirements of anticipated expansions.

ANE recommended that the Board either retain the RH-003-2011 Decision's tolling and service design framework, or adopt ANE's tolls proposal, which builds upon the Compliance Tolls but changes assumptions on billing determinants and throughput. ANE noted that it would be appropriate to consider significant methodological changes, including potential segmentation of the system, at the end of this fixed-tolling period. Further, ANE suggested that this allows for concurrent consideration of the impacts associated with the potential redeployment of assets to support the Energy East Project and reflect the benefits of the substantial depreciation of the NOL over the existing toll period.

ANE's proposal recommended that the Compliance Tolls be reduced for the remainder of the fixed toll period to reflect the early elimination of the TSA balance and incremental firm service contracting by crediting the actual positive TSA balance at the end of 2014 to the LTAA and by eliminating LTAA deferrals for the remaining three years of the period. ANE stated that this appropriately returns a portion of the excess revenues to customers through a reduction in the Compliance Tolls and avoids excessive revenue recoveries above revenue requirements during the next three years. ANE suggested that continuing tolls at current levels is reasonably likely to contribute to excessive intergenerational inequities as the current shippers would contribute

revenues far exceeding current costs. Furthermore, excess revenues would also trigger large increases in income tax responsibility.

ANE proposed to calculate net revenues consistent with the RH-003-2011 Decision. Annual differences in net revenues less any incentives paid to TransCanada would be credited to the LTAA to be reflected in the rate base utilized to set tolls for the period beginning 2018. The incentive thresholds would be updated to reflect the revised tolls.

ANE's proposed toll levels also assumed that:

- the remaining LTAA balance is amortized over three years through 2017;
- the TransCanada Contribution is eliminated;
- ROE and capital structure is as per RH-003-2011; and
- DMR for each year is equal to level reflected in the Compliance Tolls ($417 million for the test year ending 31 December 2013.)

Should its proposed tolls be implemented, ANE proposed to retain off-ramps if (i) the LTAA, positive or negative, reaches one ninth the size of TransCanada's rate base, (ii) TransCanada expects that the LTAA balance will become unrecoverable, or (iii) TransCanada disposes of or repurposes significant assets. However, any filing to address an off-ramp should be focused on resolving the situation that gave rise to that off-ramp. For example, a positive LTAA balance that reaches one-ninth the size of TransCanada's rate base should be addressed through an off-ramp application that reduces tolls.

ANE's proposed tolls reflect an Empress to Union SWDA toll of $0.95 per GJ. In its view, this toll level further enhances Mainline competitiveness as envisioned in the RH-003-2011 Decision. ANE noted that, while the Eastern Triangle is generally recognized as being the healthiest segment of the Mainline, the implementation of the RH-003-2011 Decision has improved the revenue situation outside of the Eastern Triangle, alleviating a portion of the costs of underutilized assets through a much higher utilization. ANE noted that if TransCanada captures opportunities resulting from market growth, existing Eastern Triangle shippers will bear less risk of the underutilized Prairies and NOL segments of the Mainline. In ANE's view, its proposed downward toll adjustment is consistent with reaching the positive TSA balance off-ramp of the fixed-toll methodology adopted by the Board.

Centra

Dr. Cicchetti stated that the Compliance Tolls should be the starting place to determine if the proposed application and new tolling approaches satisfy the widely accepted regulatory and economic criteria. He concluded that the proposed tolls do not satisfy the criteria that tolls shall be just and reasonable and not cause unjust discrimination. Dr. Cicchetti recommended that alternative tolling for the capital project that does not affect customers not benefiting should be considered, and emphasized that it should not be assumed that segmentation will be approved.

MAS

MAS explained that an outcome of the RH-003-2011 Decision was uncertainty surrounding future tolling and cost recovery for the Mainline, given that the shift from long-haul to short-haul transportation service decreases TransCanada's revenue, and MAS members' interest is in acquiring more short-haul capacity.

Northland

Northland argued that the Board should reject TransCanada's request to increase tolls. In Northland's view, nothing has changed to render the tolls approved in RH-003-2011 to no longer be just and reasonable or no longer at the reasonable upper limit of a competitive toll.

TransCanada's Reply

TransCanada stated that ANE's position to maintain the Compliance Tolls ignores that an off-ramp to the RH-003-2011 Decision has been reached. TransCanada stated that when ANE does acknowledge the off-ramp, it insists that any change in tolls resulting from an off-ramp having been reached should rely on historical data, such as the TSA balance, and ignores relevant facts and expectations related to market evolution over the period for which tolls would be set, such as those that would result from TransCanada making new Mainline infrastructure investments.

TransCanada noted that Centra ignores the impetus for the changes proposed in the application, and ANE dismisses the issues that gave rise to the Settlement through its stated disagreement to the fact that the RH-003-2011 Decision results in tolls that are inadequate for TransCanada to recover new capital investment. TransCanada pointed out that ANE's position ignores the evidence that Mainline revenues would be expected to fall to approximately half of the revenue requirement in 2017 in a scenario where investments that facilitate conversion to short haul were to occur under the Compliance Tolls.

TransCanada submitted that retaining the RH-003-2011 decision model, as suggested by ANE and Centra, would increase the potential for extended litigation, uncertainty, bypass and thus longer-term harm to the Mainline. TransCanada noted that this would be contrary to the Board's statements that TransCanada has a duty to protect the long-term viability of its system. Therefore, TransCanada concluded that it is not in the public interest to retain the existing model without reasonably addressing the longer-term cost recovery and tolling implications.

TransCanada stated that ANE's DMR forecast is unreasonable. TransCanada observed that the level of DMR that ANE assumed in conjunction with the firm contract levels does not reflect the evolving market dynamics including increased Marcellus production that is resulting in a transition of long-haul to short-haul contracts; fewer deliveries to export points; new receipts at these export points; and more normal weather. Rather, TransCanada observed that DMR levels could potentially be lower than that assumed in the application, which is supported by the throughput outlook information.

TransCanada estimated that implementation of the ANE tolling model would result in an under-recovery of almost $2 billion over the 2015 to 2017 period, assuming ANE's unrealistically low tolls are implemented and the proposed forecast of firm billing determinants, DMR and costs materialize. TransCanada observed that this outcome would have dramatic negative impacts on it

and parties contracting on the Mainline in 2018 and beyond. TransCanada suggested that this revenue deficit cannot be simply recorded in the LTAA for disposition in 2018 or beyond. TransCanada recommended that the Board reject the ANE tolling proposal because it results in tolls that are neither just nor reasonable, and recommended that the Board reject any conclusions drawn by ANE based on its toll proposal, including comparisons to TransCanada's proposal.

6.2 TransCanada's Proposed 2015 to 2020 Tolls

Views of TransCanada

TransCanada proposed that the Compliance Tolls remain in effect until 31 December 2014 and that the proposed tolls would be derived as a percentage of Compliance Tolls for the 2015 to 2020 period. The adjustments to the Compliance Tolls are proposed to ensure that the Eastern Triangle recovers Eastern Triangle costs and that any remaining system costs are recovered by all system users. Furthermore, the proposed tolls would be averaged and fixed for the six-year period, absent any changes that may be made during the toll review prior to 2018.

Given the proposed methodology, the toll impact on three categories of shippers was derived: Eastern Triangle Short Haul, Eastern Triangle Long Haul and Other.[4] These toll impacts are shown in Table 6-1.

Table 6-1 Proposed Tolls for 2015 to 2020 as a Percentage of Compliance Tolls

	Step 1	Step 2	Step 3	% of Compliance Tolls[5]
Eastern Triangle Short Haul	132%	120%	96%	152%
Eastern Triangle Long Haul	105%	115%	97%	118%
Other	100%	115%	97%	112%

TransCanada submitted that proposed tolls would continue to result in shippers, over the same route and under substantially similar circumstances, being charged equally. TransCanada explained that the cost allocation among energy and energy-distance components as approved in the RH-003-2011 Decision was maintained (approximately 16 per cent energy and 84 per cent energy-distance) because the proposed tolls are determined as a percentage of Compliance Tolls.

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[4] Eastern Triangle Short Haul is defined as any transportation path with a receipt point east of, and including, North Bay Junction (NBJ) and/or St. Clair to any delivery location on the Mainline. Eastern Triangle Long Haul is defined as any transportation path with a receipt point west of, but not including, NBJ and/or St. Clair and delivering east of, but not including, NBJ and/or St. Clair. Other transportation is defined as any transportation path that does not fall into the categories of Eastern Triangle Short Haul or Eastern Triangle Long Haul.

[5] As stated previously, in Undertaking 7, TransCanada provided updated costs and tolls resulting in a slight change to these percentages.

Eastern Triangle Recovery of Eastern Triangle Costs (Step 1)

Step 1 of the proposed tolling methodology ensures that the Eastern Triangle toll recovers the Eastern Triangle costs. TransCanada estimated an allocation of costs across the system (the revenue requirement) among the three segments, as well as the expected revenues, to identify the specific costs and revenues associated with the Eastern Triangle. Segmented costs, by individual cost item, were derived for each year of 2015 through 2020 using four methods: geographical, ratio of rate base, gas plant in service, and 50 per cent energy and 50 per cent energy-distance. Revenues by segment were also estimated to derive revenues for each of the three segments. TransCanada submitted that the objective of segmentation is not to increase the share of overall system costs to Eastern Triangle shippers; rather, it is to establish tolls that reflect cost causation principles in the transition to segmented tolling.

TransCanada's view is that segmentation reflects the expectation of the shift to intra-segment shipping, where shippers will be increasingly using service within a single segment as opposed to the more traditional longer-haul service spanning multiple segments.

System Recovers Remaining System Costs (Step 2)

The Step 2 toll adjustment ensures that the entire Mainline recovers all remaining system costs, including costs not already recovered by the Compliance Tolls. These remaining costs do not include costs associated with the Eastern Triangle which were accounted for in the Step 1 calculation. The Step 2 calculation recovers costs for the Bridging Contribution. TransCanada identified two groups of shippers for the Step 2 calculation: short-haul Eastern Triangle shippers; and all other shippers, including Prairies and NOL shippers and long-haul Eastern Triangle shippers.

TransCanada proposed to allocate the Bridging Contribution among the two identified groups based on their relative proportion of firm service energy billing determinants to total system firm service energy billing determinants. TransCanada explained that this allocation was appropriate because it recognizes the evolution of the system from primarily a long-haul carrier to a shorter-haul, intra-segment carrier, making distance less relevant. Additionally, TransCanada noted that the Bridging Contribution reflects undefined costs of the Western Mainline not otherwise recovered by the Compliance Tolls, and because the Compliance Tolls were established below the level that would have recovered costs in the present period, there is no way to determine what specific costs are included in the Bridging Contribution, the drivers for those costs, nor the degree to which those costs are related to distance.

TransCanada stated that if only Step 1 were implemented, the remaining system costs of approximately $1.9 billion over the 2015 to 2020 period would remain unrecovered. TransCanada noted that a deferral of that magnitude, without a mechanism that provides a reasonable opportunity for cost recovery, would have significant negative consequences and would not be appropriate.

Averaging Tolls (Step 3)

TransCanada proposed a final toll change in order to average and fix the tolls for the 2015 to 2020 period. As a result of Step 3, TransCanada submitted that an over- or under-collection of revenues will result in any particular year due to the difference in revenues collected from the average tolls versus the revenues that would have been collected had annual tolls been in place, such that a final toll adjustment is required to balance revenues to costs over the period and also to reflect the return and associated tax on return as a result of the over- or under-collection from averaging. TransCanada proposed to allocate this return and tax among eastern short-haul shippers and all other shippers, including eastern long-haul shippers based on their relative proportion of firm service energy billing determinants to total system firm service energy billing determinants.

TransCanada stated that averaging tolls in Step 3 provides toll stability for the benefit of shippers, and extends this period of stability until 2020, relative to the Compliance Tolls. TransCanada observed that this would be consistent with the Board's user-pay and no acquired rights/acquired obligations principles and promotes economically efficient price signals. TransCanada noted that a shipper pays transportation costs for the period in which they were receiving transportation service, and that paying a levelized toll is reasonable in terms of intergenerational equity and observed that this is not substantially different than the deferral of costs for future recovery that has been utilized on the Mainline for many years, including the LTAA approved by the Board in the RH-003- 2011 Decision.

Views of Participants

ANE

In ANE's submission, the application's different treatment of Eastern Triangle shippers is inappropriate. ANE noted that shippers have borne the costs and risks of previous throughput declines, and the RH-003-2011 Decision indicated that Mainline tolls should not continue to increase in order to address the competitive situation on the Mainline and TransCanada should not look to regulation to shield it from its fundamental business risks. The toll adjustments proposed by TransCanada that single out Eastern Triangle shippers shift costs and risks to shippers and shield TransCanada from the business risks that it faces.

ANE discussed concerns on how costs of providing service on each segment were determined. ANE noted that a flaw in TransCanada's approach of using estimated costs rather than a calculation of annual costs by segment is the failure to properly consider the impacts of underutilized assets, and that the significant level of unsubscribed capacity on the NOL and Prairies segments results in improper allocations.

ANE stated that TransCanada's proposed cost allocation methodology contrasts in material respects with the currently approved cost allocation methodology. ANE noted that the proposal results in a new toll for a given path that is derived from a series of differentiated percentage adjustments to existing tolls. Furthermore, as the Mainline revenue requirement is not classified between energy and energy-distance, ANE noted that there is no derivation of uniform energy and energy-distance cost components. ANE suggested that the new methodology proposed by TransCanada employs steps that reflect disparate treatment of various users of the system but that TransCanada does not provide an adequate basis for doing so.

For example, ANE showed that, when examining the year-by-year changes in specific costs assigned to the Eastern Triangle, while total OM&A costs increase by 2 per cent each year, OM&A costs assigned to the Eastern Triangle segment increase by 29 per cent from 2015 to 2016 and by 51 per cent from 2015 to 2017. ANE concluded that this is inconsistent with the results that would be achieved from an allocation of Eastern Triangle costs to the Eastern Triangle based on cost causation. The impacts of the improper treatment of underutilized capacity apply to a number of cost elements and are pervasive across the years of its forecast of costs.[6]

Centra

Centra stated that the proposed Bridging Contribution increases tolls above Compliance Tolls, thereby reducing TransCanada's risk and contributes to a shared cost recovery responsibility among shippers based on full cost of service recovery. However, the application does not establish whether this reversion to full cost recovery is fair or in the public interest.

Dr. Cicchetti suggested that the proposal's toll increase would not be just and reasonable and would violate the principle that the "beneficiary pays" because the effect would be to shift a portion of the Mainline revenue requirement from the MAS members to Western Mainline shippers that gain nothing from the eastern market area investments that TransCanada would make. Dr. Cicchetti recognized that the 12 per cent toll increase for Western shippers is not related solely to the cost of the Eastern Triangle infrastructure expansion, but also contributes to recovering the overall cost-of-service revenue requirement not met by Compliance Tolls.

MAS

MAS suggested that it is not reasonable for some shippers on the Mainline to claim that the prices they currently pay should not increase because this position does not take into account the larger context of the Mainline. MAS pointed out that the prices for all shippers on the Mainline accompany an entire costing and tolling package arising out of previous Board actions that left some long-term issues unresolved. Therefore, it is not reasonable for shippers to escape the larger consequences of the resolution of those issues by claiming that their current tolls cannot increase. To do so would appear to be claiming the acquisition of a right to a particular toll that was part of a previous Board decision with many moving parts - some of which would have affected all shippers.

TransCanada's Reply

In response to the positions advanced by ANE and Centra, TransCanada stated that its proposed cost allocation for both the 2015 to 2020 period and the tolling parameters proposed for the post-2020 period appropriately reflect cost accountability under the current and expected future use of the system. In TransCanada's view, the proposal provides for an orderly transition from the traditional integrated system tolling methodology to a segmented model in the context of the balance achieved in the Settlement.

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[6] OM&A costs are based on 50 per cent energy 50 per cent energy-distance. This change is based on the fundamental change in the billing determinants in these years (such that this increase to Eastern Triangle shippers using a segmented approach would happen anyways).

TransCanada reiterated that the proposed changes build on the existing Compliance Tolls and therefore preserve cost allocation aspects of the RH-003-2011 Decision, such as the energy / energy-distance cost allocation within tolls. TransCanada noted that the tolling approach reflected in the application is similar to that used by the Board in establishing the Compliance Tolls, where surrogate tolls were calculated under the Board-approved toll design and then adjusted by a fixed percentage to achieve an Empress to Union SWDA toll of $1.42/GJ. TransCanada proposes to adjust Compliance Tolls by a fixed percentage as well.

TransCanada advanced that the changes will also ensure that tolls for the Eastern Triangle recover the Eastern Triangle costs as well as a portion of the Western Mainline costs through the Bridging Contribution. These outcomes are appropriate considering shippers' migration to short-haul and request for service within the Eastern Triangle, and the proposed transition to a segmented toll structure where Eastern Triangle shippers will benefit from new infrastructure and increased access to supply closer to market.

TransCanada stated that Western Mainline shippers will benefit from the proposed new infrastructure in the Eastern Triangle, since absent resolution of the infrastructure issue achieved by the application, which includes the construction of new facilities in the Eastern Triangle, and the commitment of MAS to retain long-haul contracting through 2020, the system faces significant risk of partial or full bypass, thus harming all remaining shippers, particularly captive shippers, and TransCanada.

TransCanada replied to concerns raised by ANE about the proposed cost allocation among segments, specifically as it relates to the allocation of OM&A costs. TransCanada noted that certain costs not directly assignable by segment require an allocation method among segments to be used, for which OM&A costs have been assigned to segments on a 50 per cent energy and 50 per cent energy-distance basis. TransCanada suggested that this allocation appropriately reflects the cost drivers for OM&A costs, both energy and energy-distance. TransCanada also observed that as the use of the system results in a higher concentration of contracts and throughput in the Eastern Triangle, it is reasonable to expect that a larger share of OM&A costs would be assigned to the Eastern segment where proportionally more of the service is being provided and consumed.

6.3 Bridging Contribution

The application specifies that the revenue requirement for the Eastern Triangle and the Western Mainline would include the amortization of a Bridging Contribution. The Bridging Contribution is intended to recover the revenue requirement shortfall associated with (i) continuing to use the Compliance Tolls for the Western Mainline from 1 January 2015 through 31 December 2020, as compared to (ii) the revenue that otherwise would be recovered if the firm services tolls for the Western Mainline were derived using the currently projected revenue requirement and billing determinants for that portion of the system. The Bridging Contribution was proposed to be allocated between firm contracts with a receipt point in the Eastern Triangle (Short-Haul Eastern Triangle) and all other service on the Mainline based on their respective contract demand, that is, energy billing determinants. In addition, the application specifies that the Bridging Contribution would be amortized and recovered from Short-Haul Eastern Triangle shippers over the 16-year period from 1 January 2015 through 31 December 2030 and from all other shippers on the system over the 6-year period from 1 January 2015 through 31 December 2020.

6.3.1 Appropriateness of the Bridging Contribution

Views of TransCanada

TransCanada submitted that market circumstances have changed substantially since the RH-003-2011 Decision was released. TransCanada was of the view that the proposed tolls represent a transition in the Mainline tolling structure consistent with the existing and expected changes to shippers' contracting practices. During this transition period, Western Mainline shippers will benefit from both the continued long-haul commitments of MAS and the fact that the difference between the Compliance Tolls and the actual Mainline costs will largely be borne by short-haul Eastern Triangle shippers through the Bridging Contribution. The relatively higher proposed tolls for short-haul Eastern Triangle shippers are necessary to allow an orderly transition from the existing integrated system to a new segmented tolling methodology post-2020. TransCanada stated that the Bridging Contribution provides TransCanada with greater certainty of recovering costs for its existing system. This is balanced by the application's lower authorized ROE, which could be as low as 8.7 per cent due to the incentive sharing mechanism. In addition, the revenue requirement for the proposed tolls reflects the annual TransCanada Contribution of $20 million after tax, for which TransCanada is at-risk to recover. Also, because the application specifies that the tolls for the Eastern Triangle after 2020 would be based on its costs on a standalone segment basis, TransCanada submitted that it is foregoing the opportunity to argue that Eastern Triangle shippers should remain responsible for the costs of the Western Mainline post-2020, and thus has cost recovery risk post-2020 for these costs.

TransCanada stated that the application provides for a transition period during which Eastern Triangle shippers will continue to contribute to the cost recovery of the Western Mainline. The Settlement is a balance of commitments that provides long-term stability and certainty of market access, and Mainline tolls that would benefit all Mainline shippers. In so doing, it would align the interests of TransCanada and its shippers and resolve litigation. The Settlement would benefit shippers on the Western Mainline, by mitigating the threat of bypass and potential future toll increases, as well as reflecting a transition to a changed tolling regime with the Bridging Contribution borne by all shippers.

TransCanada stated that the application recognizes the historical evolution of the Mainline. The Mainline was constructed to move gas for the mutual benefit of western producers and eastern markets through the ability to buy and sell gas between these locations. It also benefited shippers along the Prairies and NOL portions of the Mainline who shared in the economies of scale that would not have existed had a system been sized only to meet their needs. The application had to recognize the MAS members share in responsibility for the recovery of costs that would remain on portions of the Mainline that they will use less as they shift to short-haul transportation.

In TransCanada's view, the RH-003-2011 Decision prevented it from building the transportation facilities MAS wanted, to obtain supplies from eastern sources to serve the immediate and growing demand in the Eastern Triangle.

As outlined by Mr. Reed, the Bridging Contribution, which provides for the recovery of Western Mainline costs from all Mainline shippers, and the MAS members' commitment to retain long-haul contracts through 2020 are linked to TransCanada's commitment to construct new Eastern Triangle infrastructure. They also mitigate cost recovery risk for TransCanada and all remaining shippers if the Mainline were bypassed.

According to TransCanada, recovery post-2020 of the unamortized portion of the Bridging Contribution applicable to Eastern Triangle shippers would not be discriminatory. Rather, recovery of these costs from the Eastern Triangle reflects the transition of the Mainline to a segmented tolling regime, and balances the fact that Eastern Triangle shippers will be provided incremental short-haul transportation.

Views of Participants

ANE

ANE submitted that the Bridging Contribution results, in part, from the conversion of excessive quantities of long-haul service to short-haul service effective 1 November 2016. While ANE opposes the Bridging Contribution on this basis, the Bridging Contribution also results from other unjust and unreasonable elements of TransCanada's revenue requirements and billing determinants, including an unrealistically low level of DMR.

In ANE's view, the non-discretionary FT service revenues and DMR are understated and lead to inappropriate conclusions regarding the need for toll increases. These same unrealistic revenue assumptions directly affect the proportion of NOL and Prairies' costs that are shifted to the Eastern Triangle. Specifically, the level of the Bridging Contribution flows directly from TransCanada's projections of FT service revenues and DMR. The Bridging Contribution is paid by all Mainline shippers, which amounts to the difference between NOL and Prairies' costs and NOL and Prairies' revenues after Eastern Triangle tolls are increased in Step 1 of the toll calculation. The Bridging Contribution and its negative impacts are estimated on a basis that is inconsistent with the current revenue situation of the Mainline.

Centra

Centra stated that while the Bridging Contribution provides for a reduction in unrecovered costs on the Mainline and thereby directionally reduces Western Mainline risk when considered in isolation, the proposed geographic segmentation of the Mainline sharply increases risk for Western Mainline shippers post-2020. The effect is the opposite for Eastern Triangle shippers. While they would pay an amortized Bridging Contribution to the end of 2030, by 2021 Eastern Triangle shippers could reasonably expect to enjoy toll reductions from a positive LTAA balance, and relative toll stability based on the revenue requirement and billing determinants of the highly utilized Eastern Triangle.

In Centra's view, the value of the Bridging Contribution does not adequately offset the post-2020 risks and uncertainties of geographic segmentation of the Mainline for Western Mainline shippers in relation to:

- Forecast underutilization on the Western Mainline;
- The significance by which the Prairies Line will not yet be depreciated;
- The magnitude of the forecast revenue requirement of the Western Mainline; and
- The toll and cost allocation methodologies for Western Mainline shippers.

Additionally, the perpetuation of unlimited pricing discretion and its effect on commodity prices for any period of the Settlement further outweighs any benefits of the Bridging Contribution for Western Mainline shippers.

MAS

MAS submitted that the role of the Bridging Contribution is part of a compromise that was needed to overcome all the various issues harming the marketplace.

The Settlement resolves an outstanding issue, as there is no reasonable prospect that the traditional gas transport patterns on the Mainline will return in the new gas market served by such abundant unconventional supplies and changing markets for WCSB supply. As was the case with transition costs for United States gas pipelines, the resolution of these costs for Canadian consumers is a reasonable part of enlisting TransCanada's participation in building new eastern capacity and resolving the uncertainty surrounding cost collection.

Union stated that the Settlement includes commitments from short-haul shippers to share a portion of the financial burden, through the Bridging Contribution for a defined period of time which will aid TransCanada in completing a balanced, staged, transition from a primarily long-haul pipeline to a more economically viable and competitive short-haul pipeline system.

Union submitted that until the Mainline is fully segmented in 2021, the Eastern Triangle is bearing a large portion of the costs of the Prairies Line and the NOL. In Union's view, the following features of the Settlement are a distinct benefit to Centra, Northland Power and other customers on the Prairies Line and the NOL:

- The RH-003-2011 reallocation of costs from distance-based to energy-based remains unchanged, increasing tolls for shippers using shorter paths;
- Through the Bridging Contribution, short-haul Eastern Triangle shippers will pay 79 per cent of the shortfall arising over the six year term of the Settlement;
- Commitments to covering the full cost of any Eastern Triangle expansions from Eastern Triangle shippers and not deferring any of these costs and assuming full responsibility for them after segmentation in 2021;
- Commitments from the three largest Mainline shippers to maintain capacity from Empress until at least 2020;
- The Eastern Triangle will cover all TBO costs associated with the GLGT backhaul contract;
- A commitment from MAS to not bypass the Mainline until at least 2030, subject to limited exceptions, ensuring their billing determinants remain on the Mainline; and
- The Eastern Triangle will absorb the LTAA post-2020, relieving the Prairies Line and the NOL of future risk relating to that deferral account.

Beyond 2020, Union fully expects to be a long-haul shipper to serve customers in western and northern Ontario.

6.3.2 Tolling Principles and the Bridging Contribution

Views of TransCanada

TransCanada stated that allocating Western Mainline costs to Eastern Triangle shippers is fully consistent with the principle of cost causation, and does not represent a cross subsidy. The Board has long approved the use of a single system-wide cost pool for developing tolls on the Mainline. TransCanada proposed to transition to a segmented tolling methodology between 2015 and 2020. However, until that transition would be complete, users of only a portion of the Mainline would, and should, continue to pay a portion of all costs on the system, regardless of the physical location of those facilities.

Mr. Reed submitted that during the 2015 to 2020 timeframe, he views the Mainline as being in a transition period, as long-haul commitments expire, intra-segment service is expanded, and tolling shifts from an integrated to a segmented system perspective. It is common under these circumstances to assign cost responsibility for transition costs across a broad customer base.

Mr. Reed concluded that applying the Bridging Contribution to all tolls, not just the Western Mainline shippers, would be consistent with the cost-based/user-pay principle. Based on TransCanada's current cost and revenue projections, continuation of the Compliance Tolls for the Western Mainline will result in significant cost deferrals. Without approval of the application, there is uncertainty regarding whether, and at what level, TransCanada will be able to recover in future tolls the costs that it will prudently incur during the fixed tolling period of the RH-003-2011 Decision. However, all shippers would benefit from the load retention and new service features of the application, and the transition to segmented Eastern Triangle tolls is an essential element of the application. Inclusion of the Bridging Contribution in tolls would reduce deferrals, help transition the tolls on the Mainline to segmented cost-of-service levels, provide TransCanada with greater certainty regarding the recovery of its prudently-incurred costs, and thus removes the obstacle that currently exists for TransCanada making new investment for the benefit of all Eastern Triangle shippers. Mr. Reed also took into account that under the RH-003-2011 Decision, Eastern Triangle shippers would have been responsible for Western Mainline costs, and found overall that recovering the Bridging Contribution from all Mainline shippers is reasonable.

Mr. Reed concluded that the application reasonably balances cost responsibility between shippers across the system. While it addresses Eastern Triangle shippers' request for additional infrastructure and increased access to short-haul Eastern Triangle service or intra-segment transportation, in his view it also establishes tolls that reasonably balance Eastern Triangle shippers' cost responsibility for existing system costs as the Mainline transitions to a new tolling methodology post-2020. Furthermore the application requires MAS to continue to use the system at least through 2030, including using long-haul for a portion of their total pipeline transportation portfolios through 2020, thus committing them to continue contributing to the cost recovery of the Western Mainline at least through 2020. Mr. Reed considered these commitments to be reasonable, given that post-2020, segmented tolls will replace the cost responsibility Eastern Triangle shippers would have had under the integrated system tolling methodology.

In Mr. Reed's view, it is not correct to suggest that shippers on the Western Mainline or in the Eastern Triangle receive no benefit from the existence of the rest of the Mainline system.

Western facilities have been used to render Eastern Triangle service, and vice versa, even when both the receipt and delivery points are located on other portions of the Mainline. In addition, the existence of the rest of the Mainline generates billing determinants that help reduce tolls across the entire Mainline, not just for service on the portion of the system that generates those billing determinants. One test in microeconomics and pricing regulation for the existence of an unreasonable cross subsidy is whether the tolls charged are above an individual shipper's standalone cost of service, that is, the costs that would have to be charged for a dedicated set of facilities designed to exclusively meet that customer's service. If a shipper's toll is below that theoretical standalone cost, then it can be shown that that shipper is benefitting from economies of scale and scope that exist from the use of joint facilities to serve the aggregate demand. Mr. Reed stated that it is likely that every shipper on the Mainline will face a proposed toll that is far below the standalone cost of providing its service, and therefore, it can be inferred that every such shipper currently benefits from the use of the integrated Mainline.

TransCanada submitted that the proposed treatment of the Bridging Contribution is consistent with the no acquired rights principle as Eastern Triangle shippers are paying for a portion of the entire Mainline's costs. This approach is consistent with the Board's approved tolling methodology for the Mainline, which has relied on a single, system-wide cost pool. The suggestion that "Eastern Triangle shippers are responsible for costs of portions of the Mainline that they are not using" is no different from a Western Mainline shipper paying for a share of the TQM TBO costs, even though that shipper may not directly use the eastern end of the Mainline. The starting point for the application's tolling methodology was the existing system-wide cost pool used to develop the Compliance Tolls, and that tolling methodology has been viewed by the Board as consistent with the no acquired rights principle.

TransCanada stated that the treatment of the Bridging Contribution does not raise any significant concerns regarding intergenerational equity. The Bridging Contribution does not involve any accelerated recovery of costs, or substantial deferral of costs, which in certain circumstances could lead to intergenerational inequities. It is recognized that, for Eastern Triangle shippers, the Bridging Contribution is expected to extend recovery of the 2015 to 2020 revenue shortfall through 2030. This would only be inequitable if it caused a substantial shift in the cost responsibility from one set of shippers to another. For example, a current shipper on the Eastern Triangle facilities could cease taking service on the Mainline during the extended cost recovery period from 2021 through 2030, thereby causing some shift in cost responsibility to other shippers. However, given the uncertainty of such an event, and the fact that the vast majority of service post-2020 in the Eastern Triangle will be provided to MAS who have committed to remaining on the Mainline at least through 2030, TransCanada stated that it does not view this as creating a material intergenerational inequity. In addition, the amortization of the LTAA as approved in the RH-003-2011 Decision occurs over a much longer timeframe.

Views of Participants

ANE

In ANE's view, TransCanada's objective, to ensure that Eastern Triangle tolls recover Eastern Triangle costs and a specified portion of the remaining system costs, treats shippers that pay Eastern Triangle tolls differently than shippers that do not, and requires Eastern Triangle shippers to subsidize others' tolls. ANE stated that these resulting discriminatory tolls for Eastern

Triangle shippers are inconsistent with the Board's tolling principles of no undue discrimination, cost-based/user pay and economic efficiency. Moreover, the proportion of non-Eastern Triangle costs to be paid by Eastern Triangle shippers results from arbitrary decisions negotiated among TransCanada and MAS.

As stated by ANE, TransCanada's toll derivation methods contribute to excessive allocation of system costs to FT service on Eastern Triangle facilities. The resulting cross subsidies are also inconsistent with the cost-based/user-pay tolling principle.

Centra

Centra explained that the proposed allocation of costs is detrimental to Western Mainline shippers because the application proposes to shelter the Eastern Triangle post-2020 from the ongoing costs of Western Mainline capacity, built as an integrated system to serve eastern Canadian and northeastern United States markets. Centra observed that TransCanada's proposal to raise existing Western Mainline tolls 12 per cent is an admission of cross subsidization because Centra and other shippers would pay 12 per cent more to finance the solution to the Eastern Triangle infrastructure problem between TransCanada and MAS. Centra observed that the new Eastern Triangle facilities are not integrated with the Mainline and proposed that they should be tolled using a standalone or incremental approach, thus removing the 12 per cent rate increase for Western shippers.

Over the 2015 to 2020 timeframe, the Bridging Contribution would temporarily contribute to a shared cost recovery responsibility by all shippers, but not to the extent necessary to level the post-2020 playing field between the settling parties and non-participating Western Mainline shippers. The series of compromises would clearly benefit the settling parties, including allowing "eastern market shippers, like the members of the MAS group, to be confident in their freedom from the responsibility for the NOL and Prairies segments as they adjust their future supply portfolios to source more supply from eastern receipt points." Western Mainline shippers would not share in this favourable outcome, which stands in stark contrast to the exacerbation of uncertainties and risks for Western Mainline shippers under the application.

6.4 Billing Determinants

Views of TransCanada

TransCanada stated that the underlying billing determinants for toll making purposes for the proposed 2015 to 2020 period included a forecast of contracts for the franchise areas of MAS that was determined based on discussions with and input from MAS. For each of the DDAs, TransCanada submitted that the current market demand was analyzed along with the potential for growth opportunities or loss of market, while respecting existing and negotiated contractual obligations, to arrive at a final forecast amount. This included MAS demand to migrate from long-haul to short-haul service to meet their needs and the negotiated minimum quantities of long-haul service to be retained.

TransCanada explained that, for other market locations, the forecast of billing determinants was determined through analysis of individual markets, which included an assessment of current market demand, potential for growth opportunities or loss of market, considered likely supply sources and the ability of a given market to meet its requirements through other pipeline systems.

Table 6-2 shows the proposed firm billing determinants by type of service for the 2015 to 2020 period.

Table 6-2 Proposed Firm Billing Determinants by Type of Service

Energy TJ/day	2015	2016	2017	2018	2019	2020
Firm	4,481	4,212	4,334	4,271	4,155	4,152
Firm Non-Renewable	269	0	0	0	0	0
Short Notice and Enhanced Market Balancing	466	487	487	487	487	487
Storage Transportation Service	791	746	740	740	740	740
Total firm	6,008	5,445	5,561	5,498	5,381	5,378

In response to a Board information request, TransCanada provided the firm billing determinants itemized by long-haul and short-haul volumes shown in Table 6-3.

Table 6-3 Proposed Firm Billing Determinants by Volume Type

Energy TJ/day	2015	2016	2017	2018	2019	2020
Long Haul Volumes	1,914	958	634	622	622	622
Other Volumes	564	590	579	559	559	559
Short Haul Volumes	3,529	3,896	4,357	4,318	4,201	4,199
Total firm volumes	6,008	5,445	5,561	5,498	5,381	5,378

Other transportation is defined as any transportation path that does not fall into the categories of Eastern Triangle Short Haul or Eastern Triangle Long Haul.

TransCanada submitted that the application's billing determinant forecast is supported by, and is consistent with, the throughput study conducted by TransCanada and the expected market

evolution due to the increasing Marcellus and Utica production. Specifically, TransCanada's forecast reflects that billing determinants will be reduced going forward as a result of the increasing northeastern United States production, resulting in less long-haul service and more short-haul service, and the anticipated decline in export flows to the northeastern United States. TransCanada's forecast was also informed by the contracting expectations over this period of the three largest Mainline shippers.

TransCanada stated that the DMR forecast for 2015 to 2020 included in the application was not based on a particular flow forecast on a path-specific basis, but instead reflects a reasonable expectation of a global amount of annual revenues that could be earned, as agreed on by the settling parties, considering the expected market circumstances in a given year, the firm contract levels already accounted for, as well as TransCanada's pricing flexibility of IT and STFT services. TransCanada stated that the forecast DMR of $180 million for 2016 is considered stretch revenue because this is recognized as an aggressive target given the heightened level of uncertainty in that year due to changing transportation dynamics in North America and particularly the northeastern United States. TransCanada explained that the majority of DMR is expected to be derived from the long-haul transportation serving eastern markets. In allocating the DMR credit to the revenue requirement among segments, TransCanada has proposed that these revenues be split evenly among the Prairies, NOL and Eastern Triangle segments. Table 6-4 shows the proposed DMR and Total Miscellaneous Revenue for the 2015 to 2020 period.

Table 6-4 Proposed DMR and Total Miscellaneous Revenue ($ million)

	2015	2016	2017	2018	2019	2020
DMR	180	180	60	60	60	60
Total Miscellaneous Revenue[7]	211	204	83	82	80	80

Given the forecasts of the MAS firm billing determinants, other shipper firm billing determinants, and miscellaneous revenues, TransCanada calculated what the overall Mainline revenues would be under Compliance Tolls, and what these revenues would be within each segment. For transportation paths that cross multiple segments, the revenues from the energy-distance component of the toll were allocated on a path-by-path basis to each segment based on the proportion of distance within each segment compared with the total path distance, using distances in accordance with the RH-003-2011 Decision. Also, for paths crossing multiple segments, the revenues from the energy component of the toll was allocated on a path-by-path basis to each segment by applying 50 per cent of the energy component revenue to the segment in which the receipt point is located, and 50 per cent of the revenues to the segment in which the delivery point is located.

[7] Includes Non-Discretionary Miscellaneous Revenues, such as Delivery Pressure and Dawn Receipt Point Surcharge and DMR.

TransCanada stated that the DMR and firm billing determinant forecasts are components of the application considered and accepted as part of the overall package by the settling parties. As a result, the DMR and billing determinant forecasts are interrelated with other components of the application, such as the toll level, the continuation of discretionary service pricing flexibility as well as the transition to increased short-haul transportation in the Eastern Triangle. TransCanada stated that modest changes to the DMR or billing determinant forecasts that are directionally consistent with the forecast in the application, would be acceptable to the settling parties and be viewed as an approval that substantially implements the terms of the Settlement.

Views of Participants

ANE

ANE asserted that TransCanada's forecast of billing determinants is not reviewable for the purposes of assessing its reasonableness and raises a material concern in the assessment of the application. ANE undertook an independent assessment of the appropriateness of TransCanada's forecast, and noted that an appropriate high level assessment results from comparing actual shipper contracting behaviour to the forecast proposed by TransCanada. ANE observed that, given TransCanada's proposed billing determinants of between 4.1 and 4.3 PJ/day, the actual shipper FT contracts prior to the beginning of the 2013-2014 winter of 5.2 PJ/day, and of the additional contracting attributable, in part, to the recent colder winter, firm contracting at the end of the winter of 6.6 PJ/day, TransCanada's proposed forecast of contracts is below the range of reasonableness for setting tolls. ANE's proposed tolls reflect a forecast of FT billing units of 5.1 PJ/day, FT short notice billing units of 0.5 PJ/day and storage transportation service billing units of 0.8 PJ/day.

ANE stated that TransCanada's billing determinants understate current contracted demand for Iroquois and East Hereford deliveries beginning in 2015, the first year of the TransCanada forecast. Based on market conditions in the northeastern United States, ANE stated that the demand for Mainline deliveries to Iroquois and East Hereford should remain strong for all years of the forecast. ANE observed that TransCanada does not reflect this demand in its billing determinants.

ANE proposed that a reasonable and appropriate basis for deriving the forecast of FT contract levels for billing determinant purposes is to rely on actual contracting behaviour since the RH-003-2011 Decision as the basis for forecasting future billing determinants. The starting point for this analysis is the FT contract levels in effect at the beginning of the 2013-2014 winter period, which equated to 5.2 PJ/day. ANE submitted that its forecast is conservative because it is not proposing to include in billing determinants over 1.0 PJ/day of FT service associated with currently effective FT contracts that were entered into for one year at some point during the most recent winter period. However, ANE suggested that the annual variations in revenues associated with these volumes should nevertheless be considered when determining TransCanada's discretionary revenues, as much of the activity may stem from shippers' willingness to pay for a full year of service to meet a need over a limited timeframe.

ANE observed that substantial elements of TransCanada's application, including its proposed tolls and the Bridging Contribution, are inextricably related to the billing determinant forecast. ANE's evidence demonstrated that the forecast is sufficiently understated to render the need for a

toll increase and the Bridging Contribution unnecessary in view of actual shipper behaviour following the RH-003-2011 Decision.

ANE suggested that the proposed DMR would lead to considerable excess revenues over the toll period, which would in turn trigger incremental income taxes and a reduction in rate base each year through contributions to the LTAA. ANE submitted that, due to other elements of the TransCanada proposal described in ANE's evidence, including understated FT billing determinants, TransCanada would already have recouped its contribution and realized incentive payments to achieve an 11.5 per cent ROE prior to the consideration of excess DMR. ANE calculated the aggregate excess DMR over the 2015 to 2020 period is $1,902 million and would lead to $493 million of incremental income taxes and a cumulative reduction in Mainline rate base of $1,543 million.

ANE's proposed tolls reflect a DMR at the same level currently reflected in the derivation of FT tolls, which is $417 million. ANE stated that this level is reasonably consistent with actual DMR since the time that the Board adopted unlimited pricing flexibility for STFT and IT services and eliminated the RAM. Given that ANE's DMR recommendation is consistent with actual DMR since the implementation of the RH-003-2011 Decision, ANE suggested that its recommendation is far less likely to lead to significant over-collections from FT tolls.

ANE explained that, given the variability in DMR from year-to-year, two to three years of experience is preferable to establish a baseline understanding of the anticipated range of DMR. ANE considered the DMR prior and subsequent to the RH-003-2011 Decision as part of its proposed DMR. ANE noted that, for 2010, 2011 and 2012, the three years prior the implementation of RH-003-2011, DMR equaled $215, $384 and $291 million respectively.

ANE proposed to impose an orderly transition from long-haul to short-haul and to recognize, to some degree, TransCanada's concerns about the resulting revenue loss, should ANE's proposed tolls be implemented. ANE suggested that 20 per cent per year for three years be allowed to convert as an example of such a transition. In response to an information request and given new information on the record, ANE revised its proposed average billing determinants for the period 2015 to 2017, reflecting its proposal to allow 20 per cent conversions of long-haul to short-haul each year beginning on 1 November 2016.

Enbridge and Union

Enbridge and Union disagreed with some of ANE's forecasts, including the DMR forecast, which appears to be based upon an extraordinarily cold winter which is unlikely to recur in each of the next six years. They also opposed ANE's proposal to convert 20 per cent of long-haul to short-haul per year for three years because, in their view, it is unfair and unworkable.

TransCanada's Reply

In response to ANE's concern that not enough billing determinant information had been provided to allow for a reasonable review, TransCanada reiterated that in response to information requests it provided a throughput analysis and a DMR outlook. TransCanada also stated that it provided itemized forecast billing determinants by path, by month, and by Mainline segment that reflect the expected MAS switch from long-haul to short-haul. TransCanada submitted that there is no merit to ANE's criticisms and that adequate information has been provided to support the

reasonableness of the billing determinants and other parameters reflected in the proposed tolls for 2015 to 2020.

TransCanada noted that ANE's forecast of billing determinants relies solely on a one-year snapshot based on existing 2014 contracts is incompatible with expectations for the 2015 to 2017 period for which ANE proposes to establish tolls, and is incompatible with actual known billing determinants for 2015. For example, TransCanada pointed out that ANE's proposed billing determinants to Emerson are unreasonably high and fail to reflect known contract information at that location, and suggested that ANE's billing determinant forecast is not reflective of anticipated evolving market trends, and does not account for the shift of Mainline contracting from long-haul to short-haul and the declining (and reversal) of export flows to the northeastern United States.

TransCanada noted that because ANE's billing determinant forecast for 2015 to 2017 is fixed at the existing 2014 contracting level, the gap between ANE's forecast and the application's widens over time, particularly in terms of energy-distance billing determinants. TransCanada suggested that this widening gap illustrates the magnitude of the issues associated with ANE's failure to reflect expected contract evolution over the 2015 to 2017 period. TransCanada observed that, all else equal, ANE's forecast of billing determinants for 2016 and 2017 relative to those reflected in the application are overstated by 69 per cent and 101 per cent, respectively. With respect to the 20 per cent annual conversion recommendation from ANE, TransCanada suggested that ANE is recommending to reduce the toll impact on all other shippers, even though in the past there were no such restrictions on long-haul to short-haul conversion and these costs were borne by all shippers.

In TransCanada's view, the DMR forecast used in the application is reasonable and reflective of anticipated developments over the period for which tolls are proposed to be set. TransCanada suggested that, in contrast to ANE's proposal, there is no basis to rely on Compliance Filing levels of DMR when future circumstances are expected to be significantly different. TransCanada noted that ANE's DMR forecast of $417 million per year fails to account for the impact of the abnormally cold 2013-2014 winter or the interaction between firm contract levels and discretionary service revenue. TransCanada observed that the market dynamics and associated contracting practices have evolved and continue to do so, but this is ignored in the ANE DMR Forecast. TransCanada suggested that this market evolution is reflected in the DMR forecast in the application, which includes $180 million/year for 2015 and 2016 and then $60 million/year for the 2017 to 2020 period.

TransCanada noted that in recent years, much of the DMR has been realized on long-haul paths from Empress. TransCanada suggested that it is expected that, in the future, a growing share of DMR will be realized on short-haul paths as a result of the addition of new facilities in the Eastern Triangle and the related increase in short-haul capacity. TransCanada noted that this transition points to lower DMR revenues in the future, and concluded that it is not reasonable to expect the 2014 level of DMR to be sustained in 2015 and beyond, let alone increased by $70 million and then maintained at that level to the end of 2017, as reflected in the ANE forecast.

TransCanada also submitted that the DMR forecast was developed under the first diversion policy included in the Settlement agreement, which had the ability to generate more revenue from diversions and therefore increase the DMR relative to the revised diversion policy included

in the application. TransCanada further noted that in a number of markets IT has not been generated at all because diversions are scheduled at a higher priority than IT.

6.5 Rolled-in tolling of new facilities

Views of TransCanada

In TransCanada's view, rolling-in the costs of the new facilities anticipated to be in-service between 2015 and 2020 into the Eastern Triangle tolls is fully consistent with the Board's prior policies regarding rolled-in tolling, which remains appropriate after segmentation. TransCanada noted that the costs of new facilities in the Eastern Triangle could be recovered, depending on the nature of the facilities constructed, either through incremental tolls, standalone tolls, and/or through the use of a contribution in aid of construction by the shippers utilizing the new facilities. However, TransCanada observed that such alternate approaches would be inconsistent with the Board's long-standing policy, described as being that the aggregate demand of the system creates the need for new infrastructure, and would not reflect the traditional integrated operations of the Eastern Triangle and the multiple paths by which deliveries are made in that portion of the system.

TransCanada noted that there are benefits associated with new facilities, such as enhanced operational flexibility and reliability. TransCanada also suggested that because the new facilities facilitate the conversion from long-haul to short-haul transportation, its business rationale needs to extend beyond cost recovery for only the new facilities, to consider the full range of impacts on TransCanada and the other shippers on the system. In its view, the application reasonably addresses these concerns by balancing the construction of new facilities in the Eastern Triangle with the opportunity for reasonable cost recovery.

TransCanada stated that if the costs of the new eastern facilities were added to the Compliance Tolls until the end of 2017 on a system-wide rolled-in basis, the resulting toll change would provide for cost recovery of the annual cost of service associated with the facilities themselves, but would not provide for the loss of revenue associated with the conversion of long-haul to short-haul that the new build facilitates. TransCanada indicated that the financial impact that results from this conversion is acceptable only in the context of the Settlement. For example, the total annual cost of service for the new facilities from 2015 to 2017 is approximately $109 million, which in turn would result in a 3.0 per cent toll increase to the Compliance Tolls. TransCanada stated that, in order to reflect the change from long-haul to short-haul for 2015 to 2017 as a result of the new facilities, tolls would need to increase by 15 per cent relative to Compliance Tolls. Considering the impact of conversion on the 2018 to 2020 time period, tolls would need to increase by 57 per cent relative to the Compliance Tolls.

TransCanada suggested that if the cost of the new Eastern Triangle facilities were allocated based on an incremental or stand alone approach or through the use of a contribution in aid of construction, the impact would depend on how the resulting toll was structured. TransCanada noted that, in order to allocate the cost of the new Eastern Triangle facilities to only those shippers using the new facilities, it would be a significant challenge to identify who those users are, given the highly integrated nature of these new facilities with the rest of the system. While the new facilities are underpinned by contracts, TransCanada noted that it is the combination of all users in this area that drive the need for the facilities, and all shippers on the system have

access to and can benefit from the new facilities. TransCanada also noted that the facilities could also be used by all shippers using discretionary services.

For the years 2021 and beyond, a term of the Settlement was that prudently incurred costs incurred for facilities constructed in the Eastern Triangle up to 2030 would be included in the Eastern Triangle rate base and tolled on a rolled-in basis.

Views of Participants

ANE

ANE stated that it supports the immediate construction of needed TransCanada facilities in the Eastern Triangle with the costs relating to such facilities being placed into a deferral account and their tolling treatment determined in a further proceeding for effect after 2017. ANE stated that its proposal to implement a deferral account for expansion-related facility costs is independent of its toll proposal and can be implemented along with its toll proposal. ANE noted that the costs of the expansions appear to be modest and may be offset by incremental revenues. ANE suggested that the Board could implement the deferral account with or without a return component. When the deferral account is reflected in tolls, it would be incorporated in rate base, including any deferred return component adopted by the Board. The income taxes on the deferred return component would be recoverable over the time period that the associated facilities are depreciated.

Centra

Dr. Cicchetti noted that just because the Eastern Triangle infrastructure investments are not integrated into the Mainline does not mean that the segmentation proposal is in the public interest or appropriate, particularly on a geographic basis. Rather, any segmentation of the Mainline should incorporate historic use or some other basis that reflects both why the Mainline was expanded and the users that benefitted from such expansions. The assignment of the costs of Eastern Triangle expansion projects does not require segmentation.

TransCanada's Reply

TransCanada noted that a tolling treatment to recover only the new Eastern Triangle facilities costs does not address the loss of revenue associated with the conversion of long-haul to short-haul that the new build would facilitate, nor does it recognize the integrated nature of the Eastern Triangle facilities. TransCanada observed that it is a long-standing Board practice to utilize a rolled-in tolling approach for new facilities that are integrated with existing facilities to serve the requirements of existing and new shippers collectively, where the nature of the service to be provided is not custom or distinct. TransCanada proposed that this applies to the new facilities being proposed in the application, and there is no basis to deviate from this long-standing Board tolling approach.

TransCanada suggested that a move toward segmented tolling does not change the appropriateness of this approach given the new Eastern Triangle facilities will be integrated with the existing Eastern Triangle facilities and the service to be provided on the new facilities is the same as that on the existing facilities.

TransCanada also countered Centra's concern about Western Mainline shippers bearing costs associated with the new facilities by stating that there is no Western Mainline shipper cost responsibility for new Eastern Triangle facilities under the application proposal in either the 2015 to 2020 transition period, or under the 2021 to 2030 segmented tolls period, because Eastern Triangle costs would be recovered exclusively from Eastern Triangle shippers. TransCanada noted that Centra, or any Western Mainline shipper, would only bear a portion of these Eastern Triangle costs to the extent it uses transportation services in the Eastern Triangle segment.

TransCanada submitted that ANE's proposal to build the facilities without a certain cost recovery plan is not a reasonable or balanced regulatory approach to resolving the existing impasse of this critical issue, but rather is completely asymmetric and imbalanced.

6.6 Views of the Board

The Board recognizes that off-ramps were included in the RH-003-2011 Decision to account for material changes affecting the Mainline. In the Board's view, such a material change in the financial position of the Mainline and to market circumstances since the implementation of the Compliance Tolls has occurred.

ANE submitted alternative tolls until 2017 based on the RH-003-2011 tolling model but which incorporated a number of changes, as described above. The Board accepts ANE's submission to require TransCanada to account for the allocation of the actual TSA to the LTAA. The Board was, however, not persuaded that ANE's proposed billing determinants, based largely on the continuation of the increased firm service billing determinants achieved in 2014 through to 2017, represent a sustainable level of revenue that should be used in the calculation of tolls. To do so would increase the likelihood of LTAA contributions and, therefore, the risk of unrecovered costs for both shippers and TransCanada. Furthermore, the Board did not find the proposed 20 per cent annual transition from long-haul to short-haul transportation to be a workable or fair model for a transition to segmentation on the Mainline.

The Board approves the applied-for firm service billing determinants and the DMR forecasts, subject to the updates discussed below. The Board is aware that by approving the application of capital additions to the Eastern Triangle rate base, thus facilitating the transition from long-haul to short-haul capacity, there is a likely net reduction in billing determinants across the Mainline. While recognizing that forecasts are inherently uncertain, the Board nevertheless considers TransCanada's forecasts to be reasonable and notes the downside risk to TransCanada, as well as to the account of shippers, should these forecasts not materialize.

The Board finds the proposed allocation of costs among the three Mainline segments to be reasonable. In the RH-003-2011 Decision, the Board observed that a segment recovering its costs is a good check on the reasonableness of a cost allocation methodology, especially when the Eastern Triangle segment is the healthiest on the Mainline. The Board is of the view that the Step 1 calculations reflect an appropriate allocation of Eastern Triangle costs to Eastern Triangle shippers, and that this step is reasonable in the context of the transition to segmentation.

Centra raised concerns about its toll increase resulting from bearing costs associated with these new Eastern Triangle facilities. While the Board was not convinced by TransCanada's evidence that these facilities directly benefit all Western Mainline shippers in the long term, the Board understands that there are no direct costs associated with the new facilities in the Eastern Triangle allocated to Western Mainline shippers.

The Board notes that market circumstances have substantially changed in recent years. The historic Mainline toll methodology reflected a single, system-wide cost pool under which service on any portion of the system pays a toll that reflects a share of the entire system's costs. For the period 2015 to 2020, the Mainline remains integrated and the Board finds it appropriate for all shippers to contribute to the recovery of total Mainline costs.

Eastern Triangle shippers have requested that TransCanada build additional facilities that would expand their access to gas supplies close to their markets. The new facilities would enable Eastern Triangle shippers to convert from long-haul to short-haul transportation and would be underpinned by initial 15-year contracts. The Board heard that TransCanada was not prepared to construct new facilities that would facilitate a drop in long-haul billing determinants without a broader solution. The Board notes that the forecasts provided in this proceeding reflect an anticipated underutilization on the Western Mainline as long-haul capacity shifts to short-haul capacity. TransCanada's proposed Bridging Contribution seeks to address the under-recovery associated with this underutilization during the 2015 to 2020 period.

The proposed Bridging Contribution seeks to balance the various interests of TransCanada and its shippers during the 2015 to 2020 transition period. The Bridging Contribution will provide TransCanada with greater certainty regarding cost recovery. Though all of the benefits to Mainline shippers are not certain, the Board acknowledges that the commitments TransCanada made in the context of developing the Settlement will result in increased capacity in the Eastern Triangle. Facilitating increased capacity is consistent with the evolution of contracting practices on the system. The Board has not evaluated the specific value of the Bridging Contribution to each Mainline stakeholder. The Board relies on the long-haul volume commitments of MAS members to aid in the realization of the proposed benefits to shippers. The Board directs TransCanada to report in the 2018 review: the FT long-haul volume commitments of MAS on the Western Mainline, the actual FT long-haul volumes contracted for on the Western Mainline, and provide an explanation of any variances.

Post-2020 toll methodologies and toll levels have not been applied for in this application. The forecast underutilization, depreciation level of the Prairies Line, forecast revenue requirement, toll and cost allocation methodologies for the Western Mainline will be the subject of a future proceeding. The Board has not made a determination on these matters in this proceeding.

The Board finds the Bridging Contribution to be appropriate in the context of the overall application. The Board approves allocating the Bridging Contribution between the Eastern Triangle short-haul shippers and all other shippers based on firm service energy billing determinants and the proposed amortization schedules. The Board heard evidence that, in other North American energy sector restructuring cases, such transition costs have

been allocated on an energy-cost basis. This provided reassurance that the allocation of such transition costs is reasonable.

The Board notes that, if Western Mainline shippers were to pay tolls reflecting the costs on the Western Mainline, the resulting tolls would be substantially higher than the proposed tolls. The Board views the toll increase for Western Mainline shippers in Step 2 as being a reasonable contribution to the Mainline in this transition period. The Board notes that the impact on Mainline's revenues could be significantly negative should the proposed tolls not be implemented, and this would result in significant cost deferrals.

The Board finds that the implementation of the Bridging Contribution does not raise intergenerational equity concerns. The Board relies on the evidence that the vast majority of service post-2020 in the Eastern Triangle will be provided to current shippers in the Eastern Triangle. The Board approves the amortization and collection of the Bridging Contribution in short-haul Eastern Triangle tolls over the 16-year period from 2015 to 2030.

Concerning Step 3, the Board finds toll averaging to be acceptable, in light of reasonably balancing shipper benefits of toll stability and certainty with intergenerational equity. The Board notes that no party submitted evidence expressing concerns with toll averaging.

Based on the above, the Board finds the proposed toll design for the 2015 to 2020 period, including the Eastern Triangle recovery of Eastern Triangle costs (Step 1), the system recovers remaining system costs (Step 2), and toll averaging (Step 3), to be reasonable. This finding is subject to the requirement that TransCanada files a compliance filing for 2015 to 2020 tolls before 31 March 2015.

The compliance filing must include the following adjustments to the proposed tolls:

- the actual TSA balance as of 31 December 2014 is to be allocated to the LTAA; and,
- all revenue requirements and firm billing determinants for 2015 to 2020 are to be updated as of 31 December 2014.

This requirement for a compliance filing necessitates interim tolls. Therefore, the proposed tolls are authorized as interim tolls effective 1 January 2015. Differences recorded due to charging the interim tolls from 1 January 2015 until final tolls are approved are to be captured in the LTAA.

The Board approves rolled-in tolling into the Eastern Triangle rate base of the Eastern Triangle capital expansions between 2015 and 2020, and approves in principle the practice of rolling-in Mainline facilities costs in the future, such that the costs of facilities additions in the Eastern Triangle will be rolled-in to Eastern Triangle tolls until 2030. The Board recognizes that rolled-in tolling has been a common practice on the Mainline, and notes the challenges in adopting an alternative tolling approach given the integrated nature of the proposed facilities in the Eastern Triangle. The Board notes, however, that each facilities application is unique and the reasonableness of continuing the practice of rolled-in tolling will be considered by the Board in its assessment of the specifics in each application.

Decision

The Board approves TransCanada's proposed toll design and requires TransCanada to file a compliance filing for 2015 to 2020 tolls by 31 March 2015.

The Board also approves rolled-in tolling into the Eastern Triangle rate base of the Eastern Triangle capital expansions between 2015 and 2020, and approves in principle the practice of rolling-in Mainline facilities costs in the future, such that the costs of facilities additions in the Eastern Triangle will be rolled-in to Eastern Triangle tolls until 2030.

6.7 Separation of costs by segment

The Settlement does not establish a specific toll design or toll level beyond 2020 for any portion of the Mainline. TransCanada requested Board approval of a tolling parameter in which all costs associated with the Eastern Triangle will be separated from the NOL and Prairies Lines, that is, the costs associated with those particular segments would be assigned to the revenue requirement for those respective segments, and thus would be recoverable independently from one another for the post-2020 period.

Views of TransCanada

TransCanada submitted that there is a transition underway where shippers in the Eastern Triangle have an increasing demand for short-haul transportation. To facilitate an orderly transition, the application proposes tolls in the Eastern Triangle that fully recover the costs of the Eastern Triangle and, through 2020, contribute to the recovery of the costs of the system as a whole. Segmentation of the Mainline post-2020 would result in Eastern Triangle tolls that reflect the changing use and cost structure of the system.

TransCanada stated that it is important that toll design be changed when a change in circumstances dictates it would be appropriate. As shippers have indicated that they intend to rely principally on intra-segment transportation in the future, there is a low probability that future utilization of the system will revert to significantly greater inter-segment transportation. Further, per TransCanada, it is beneficial for TransCanada and all shippers that use of the existing Mainline system be maximized; under current market conditions, however, it is likely that increases in utilization will primarily be driven by increases in intra-segment service rather than inter-segment service. This indicates that the Mainline's existing integrated system toll design may no longer be appropriate.

TransCanada submitted that the proposed 2015 to 2020 tolls and segmentation post-2020 appropriately reflect cost accountability when taking into account shippers' current and expected future use of the system, and enable Eastern Triangle shippers to benefit from new infrastructure and increased access to supply closer to market.

TransCanada stated that Mainline tolls post-2020 would be determined in a future proceeding, based on the circumstances prevailing at that time. Given that approval of the application would fix tolls from 2015 through 2020, there would be ample time for consultation between TransCanada and its stakeholders about the most appropriate segmented tolling regime and toll level for the Mainline beyond 2020, and for the Board to make a determination of just and reasonable tolls for that period.

Mainline tolls after 2020 could reflect a number of factors, including developments beyond cost-of-service regulation that would address fundamental allocations of risk and reward between TransCanada and its shippers. Although in this application TransCanada is only requesting the Board's approval of certain parameters for tolls in the 2021 to 2030 period, TransCanada stated it remains committed to continuation of balanced and effective at-risk models for some or all of the Mainline's revenue requirement.

There are many variables that are relevant to the specific tolls post-2020 that still need to be determined and approved by the Board in order to set future tolls on the Mainline. For example, there has been no determination on the specific cost allocation for any portion of the Mainline post-2020 (for example, allocation between the energy and energy-distance components of the toll). Further, it has not been determined whether it would be reasonable to consider the Western Mainline as one or two segments for toll design purposes after 2020. Approval in this proceeding of the tolling parameters will not constrain the Board's future determinations of whether Mainline tolls for a given period are just and reasonable and not unjustly discriminatory, nor constrain TransCanada or its stakeholders from advancing proposals for fundamental changes that entail a more substantial departure from cost-of-service tolls.

As outlined by TransCanada, segmented tolls would continue to result in shippers over the same route, under substantially similar circumstances, being charged equally. Segmented tolls would not result in undue advantage or disadvantage to any particular shipper or group of shippers relative to similarly-situated shippers. Therefore, segmented tolling would produce tolls that are not unjustly discriminatory.

TransCanada stated that segmented tolling is consistent with cost causation. Under segmented tolling, shippers using specific segments of the system will pay the costs for those segments, including the TBO costs used to facilitate transportation for a particular segment. Furthermore, infrastructure improvements and expansions in each segment will be paid for by those parties using each segment. Under this revised tolling methodology, shippers whose service is limited to intra-segment service will largely be unaffected by changes in costs, billing determinants or the service mix on other portions of the system.

TransCanada stated there is uncertainty about whether the Western Mainline will be able to recover sufficient revenues to meet its revenue requirement after 2020 and that a different tolling model may be appropriate for the Western Mainline post-2020. This tolling model would be the subject of future discussions between TransCanada and shippers and of a subsequent application prior to 2021. TransCanada submitted it is premature for the parties to debate, and for the Board to now determine, whether there will be stranded costs post-2020 or how to determine responsibility for those costs.

In argument, TransCanada addressed the Board's authority to approve the tolling parameters that would remain in effect until 2030. TransCanada stated that a regulatory tribunal will not be bound in the future by what the previous tribunal had said. TransCanada recognized that the actual tolling methodology post-2020 would be the subject of a future proceeding as the doctrine of *stare decisis* does not apply in this context. TransCanada requested only an indication from the Board now regarding the tolling parameters under the current circumstances.

Views of Participants

ANE

ANE stated it was strongly opposed to the segmentation proposal put forth by TransCanada. The proposed methodology will be applied inconsistently among the Eastern Triangle and other Mainline segments, fails to properly address the impact of underutilized assets for categories of costs that are allocated among segments, and is driven by unrealistic assumptions, including overstated rate base and understated DMR. Further, the segmentation proposal needed to address the economic impacts of constructing facilities to accommodate the growth requirements of MAS. Given the substantial increase in tolls that results from the proposal, ANE sees no reason to base a further change in tolling methodologies upon TransCanada's segmentation proposal.

Centra

Centra stated that its primary opposition is to the proposed segmentation of the Mainline because it facilitates the shifting of long-term costs and TransCanada's fundamental risk to Western Mainline shippers.

Centra submitted that the Mainline was built largely to serve eastern Canadian and northeastern United States markets yet the application proposes to allocate all Prairies Line and NOL capacity and associated costs to the Western Mainline under segmentation. It would appear that by facilitating the abandonment of long-haul contracts in exchange for Eastern Triangle short-haul capacity, captive Western Mainline shippers would be left to pay for large amounts of capacity that was not built for them, that they have never used and for which they have no use going forward.

Centra indicated that the need for Mainline segmentation has not been articulated in the application. Centra's witness, Dr. Cicchetti, believes a separate Board process would be required to establish the prudence of such a fundamental and enduring change, including consideration of the appropriate basis of segmentation and related cost allocation and tolling methodologies outside the operationally integrated Mainline.

Centra submitted that if segmentation is approved now in principle, it would be a *fait accompli* prior to the determination of related fundamental issues such as cost allocation, recovery, liability and toll methodology. The extent to which things could be made "right" for captive shippers and their end-users would be limited and there could be no opportunity to undo harm in the event that examination of these fundamental issues in a future tolls hearing results in the determination that segmentation was neither appropriate nor necessary. To rule on the necessity and reasonableness of segmentation requires information about all of these future considerations.

Centra stated that the Mainline segmentation proposal assumes that geographical segmentation would be appropriate. Although Centra opposes segmentation, if it is to be considered then various approaches to segmentation must be evaluated and presented for consideration. For example, it has been acknowledged that the Mainline was built primarily to serve eastern markets. It would be appropriate to consider allocating to the Eastern Triangle the cost of at least two-thirds of Mainline capacity from Empress to both Emerson and North Bay Junction. This could be accomplished relatively easily as, for the most part, six individual pipelines comprise the Mainline from Empress to Station 41, from which three pipelines extend to each of Emerson

and North Bay Junction. Contemplating this and other potential alternative approaches to Mainline segmentation is necessary to conclude whether segmentation is appropriate and reasonable. Without sufficient clarity and certainty as to the parameters and thresholds for future cost recovery and liability and that any future legal challenge(s) of disallowed costs would be unsuccessful, it would appear that segmenting the Mainline on the basis of geography would be the worst possible approach.

In Centra's view, the option of Eastern Triangle short-haul billing determinants and resulting tolls contributing to cost recovery on the Western Mainline would be lost, potentially forcing unprecedented decisions as to specific cost recovery liability and the disallowance of Mainline costs (which may face legal challenges) in lieu of significant toll increases for the remaining Western Mainline shippers.

Limitation of the Board's options in resolving cost recovery issues associated with underutilized Mainline assets, coupled with evidence of the continued operational integration of the Mainline and historical under-recovery of Eastern Triangle costs from the Eastern Triangle segment, demonstrates the flaws inherent in the proposed segmentation of the Mainline.

Centra stated that after the 2020 transition, this would strand assets that are primarily on the newly formulated Western Mainline. This would mean that the application would effectively assign the responsibility for stranded Mainline costs to captive Western Mainline customers and shareholders.

As outlined by Centra, the application shifts cost recovery risks and burdens to Western Mainline captive customers and provides MAS with an exit from long-haul FT Mainline services. If adopted, the use of exit fees should be considered as part of any such major restructuring.

Centra stated that the application left the future sharing of costs undetermined between Western Mainline shippers and TransCanada shareholders once the Western Mainline is severed from the healthy Eastern Triangle. The appropriateness of any segmentation, and geographic segmentation in particular, can only be determined if the liability for under-recovered costs would be fully considered. While departing customers or segments are still part of the system, this consideration should be at the conceptual level, and happen after an examination of real costs, triggers, and thresholds. Deferring these determinations post-departure will limit the options of the regulator and increase the likelihood of unfair outcomes for a small number of remaining shippers.

If segmentation is to be approved, then the cost causation/user-pay tolling principle should apply such that Western Mainline shippers like Centra are shielded from undue obligations for Western Mainline costs resulting from geographic segmentation. This would require a determination of the extent to which Western Mainline assets are used and useful, to ensure that the appropriate parties bear the appropriate cost responsibility. Postponing the resolution of this fundamental issue to a future date while seeking NEB approval to segment the Mainline and shield the Eastern Triangle from cost liability for these underutilized assets today is not a reasonable or appropriate proposal.

Review and consideration of used and useful, including the tolls that would result from this determination, may be more effectively conducted when there is definitive information on the impacts of the Energy East and associated Eastern Mainline projects on Mainline rate base. Centra submitted that TransCanada steadfastly denies that its shareholders bear any responsibility for stranded costs.

Gaz Métro

Gaz Métro stated that TransCanada recognized a potential issue could be the absolute level of tolls in the Prairies segment post-2020. However, TransCanada said it would be prepared to assume the risk associated with this. In other words, if it was decided one day that under the principles established by the Board, tolls in the Prairies segment were too high, TransCanada would have to propose solutions acceptable to the regulator, but in no case could it ask eastern shippers, who would no longer be using long-haul, to mitigate its risks as identified in the RH-003-2011 Decision.

MAS

MAS submitted that TransCanada has acknowledged that it remains subject to the risk of a cost disallowance on Prairies Line after 2020 and that it finds the risk of the $1 billion investment in the Western Mainline post-2020 bearable compared to a $5 billion or $6 billion investment today. The application does nothing to diminish the following basic protection against excessive tolls for the Western Mainline as outlined in the RH-003-2011 Decision, p.233:

> *(the Board) concern related to future shippers' potential exposure to deferred costs is mitigated because we have found that Mainline tolls cannot continually increase each year in response to throughput declines*

Shippers on each of the Prairies Line, NOL and Eastern Triangle can take comfort in that basic fact.

MAS stated that it is important for eastern market shippers to know that there is a limit to any exposure to the cost of remaining capacity outside the Eastern Triangle that is no longer utilized for service on that segment of the Mainline. The segmentation of the costs of the Mainline permits eastern market shippers, including MAS, to be confident in their freedom from the responsibility for the NOL and Prairies segments as they adjust their future supply portfolios to source more supply from eastern receipt points.

MAS submitted that segmentation is consistent as a foundational cost allocation principle in the application first because it would be entirely consistent with recognizing the cost to serve shippers who seek service on any or all of the three segments of the pipeline. The integrated tolling framework, on the other hand, fails to recognize that some shippers, such as Centra, are only served from one segment of the Mainline with different characteristics than shippers physically located off the other segments of the Mainline. Second, the adoption of segmentation as a cost allocation principle would not dictate a particular rate design or rate setting approach. To the extent that different segments of the pipeline exhibit different utilization characteristics, segmentation would allow for the tailoring of the most appropriate rate setting methodology for the segment. Finally, segmentation would also be more consistent with the current evolution of the natural gas industry in North America where production and markets are becoming increasingly regionalized. However, should supply preferences change, markets in eastern Canada could be served from western Canada by paying tolls for the segments servicing them. The converse would not be true of the existing integrated tolling methodology which ties the willingness to invest in infrastructure to long-haul paths and therefore creates tension between the pipeline operator's willingness to serve and shippers' freedom to choose their supply sources.

6.7.1 Timing of Segmentation

Views of TransCanada

TransCanada says that implementation of the tolling parameters proposed in the application is essential now to resolving immediate and important issues. Approval of these parameters will not constrain the Board's future determinations as to whether Mainline tolls for a given period are just and reasonable and not unjustly discriminatory, nor constrain TransCanada or its stakeholders from advancing proposals for fundamental changes that entail a more substantial departure from cost-of-service tolls.

In TransCanada's view, approval of segmentation of the Eastern Triangle starting in 2021 as part of the application would not compromise the Board's ability to establish just and reasonable tolls for the Western Mainline in the future. Mainline tolls after 2020 could reflect a number of factors, including developments beyond cost-of-service regulation that would address fundamental allocations of risk and reward between TransCanada and its shippers. TransCanada remains committed to continuation of balanced and effective at-risk models for some or all of the Mainline's revenue requirement and reaffirmed this during the hearing.

Views of Participants

ANE

In ANE's view, significant methodological changes, including potential segmentation of the system, would be appropriately considered at the conclusion of the Compliance Toll period in 2017. This would allow for concurrent consideration of the impacts associated with the potential redeployment of assets to support the Energy East Project and reflect the benefits of the substantial depreciation of the NOL over the existing toll period.

ANE stated that the changes to tolls and services adopted by the Board in the RH-003-2011 Decision are dramatically affecting the utilization of the Mainline and its economic condition. The steady state of these changes is uncertain; however, additional time operating under the current tolling framework would add considerable clarity. Presumably in late 2016 or early 2017, TransCanada would bring a settlement or application to the Board for tolls to be effective at the conclusion of the existing fixed-tolling period adopted in the RH-003-2011 Decision. By that point in time, three plus years of actual experience operating under the parameters of the RH-003-2011 Decision would provide a greater understanding of anticipated utilization of the Mainline, including by FT shippers, and of TransCanada's ability to generate discretionary revenues. This experience would be invaluable to the conception and development of potential changes to tolling methodologies that are sound and satisfy the Board's tolling principles

Centra

Centra submitted that the application was not simply a means of allowing for Mainline investment and improving market access and supply diversity, as Mainline segmentation would not in any way be required to achieve these goals. Segmentation shifts cost responsibility for significantly underutilized Mainline assets, while its proponents maintain that there are no alternatives or that the ultimate cost responsibility would lay with TransCanada. At the same

time, the Eastern Triangle receives assurances on limits on cost exposure for underutilized assets that were built to serve them. All of this must also be considered in light of the fact that the Western Mainline is struggling today and may be significantly worse off tomorrow.

Centra stated that the Prairies Line, the NOL and the Eastern Triangle would not be depreciated by the end of 2020, the timeframe after which segmentation of the Mainline is being proposed. This brought into question the appropriateness of the segmentation proposal in the application.

In Centra's view, a geographic or other segmenting of the Mainline without any prior determination of segmented tolling and cost allocation methodologies would be an inappropriate outcome post-2017. The segmentation proposal, like the entire application, was based solely on a closed and thus unfair negotiation.

6.7.2 Views of the Board

The Board has heard from numerous parties in this proceeding regarding the rapidly evolving natural gas market and the uncertainty anticipated in the next few years. The development of the Marcellus and Utica regions has had a significant effect on the natural gas marketplace in North America. The Board notes the changes in market circumstances and the evolving contracting practices indicate a greater preference for intra-segment transportation in the future.

The segmentation tolling parameter is one component of the application. The Board has not considered details regarding segmentation including negotiated exit fees, forecast post-2020 level of throughput, potentially stranded assets, cost allocation, post-2020 toll design, post-2020 toll components, or the impact of future projects, including Energy East. These issues will all be the subject of future proceedings. TransCanada has committed to consult with its shippers to establish the most appropriate segmented tolling regime. The Board further notes TransCanada has also committed to balanced and effective at-risk models for some or all of the Mainline's revenue requirement. The Board reiterates that tolls cannot continually increase each year in response to throughput declines. The Board anticipates that TransCanada will be incented to provide competitive tolls post-2020 on the Western Mainline. This may include tolls below the cost of service or tolls determined according to other at-risk tolling methodologies.

The segmentation tolling parameter relates to a future period and approval in this proceeding of the requested segmentation tolling parameter would not constrain in any way the Board's future determinations as to whether Mainline tolls for a given period are just and reasonable and not unjustly discriminatory.

Based on the current circumstances, the Board approves the segmentation tolling parameter in principle at this time and will continue to monitor the appropriateness of the segmentation tolling parameter prior to implementation. Should circumstances be significantly different approaching 2020, the Board would expect the issue of segmentation to be re-examined to determine if it remains appropriate.

Decision

The Board approves the segmentation tolling parameter in principle at this time and will continue to monitor the appropriateness of the segmentation tolling parameter prior to implementation.

Chapter 7

Risks and rewards

7.1 Fair Return

Views of TransCanada

In its application, TransCanada proposed that the Mainline's ROE be set at 10.1 per cent from 2015 until the end of 2020. Additionally, TransCanada proposed to maintain the 40 per cent equity ratio approved by the Board in RH-003-2011.

Fair return standard

According to TransCanada, the level of ROE specified in the application was not based on a *de novo* assessment of risk derived from an application of the fair return standard. Instead, it was a negotiated level, consistent with the allocation of risks in the overall settlement package agreed to by the settling parties. TransCanada added that the applied-for return was based on negotiations between sophisticated parties, and that several other pipelines have negotiated the same ROE.

TransCanada was of the view that the Board had the information on the record that was necessary for it to approve the proposed return, 10.1 per cent on 40 per cent equity, as being within the range of returns that meet the requirements of the fair return standard.

Capital market conditions

TransCanada submitted that certain inputs into cost of capital models had decreased from the time that the RH-003-2011 fair return evidence was prepared until the time the RH-001-2014 application was submitted. Among these indicators were the risk free rate decreasing from 3.8 per cent to 3.2 per cent and the GDP growth rate estimate falling from 2.6 per cent to 2.3-2.5 per cent. According to TransCanada, using these as inputs into the Capital Asset Pricing Model (CAPM) or the Discounted Cash Flow model (DCF) would lead to directionally lower ROE estimates compared to when the RH-003-2011 evidence was prepared.

TransCanada submitted an update to some of the samples used for its risk positioning model it provided in the RH-003-2011 proceeding. Based on the updated sample, the comparable ROEs had declined by about 50 to 70 basis points (bps) from June 2011 to December 2013. While this update only had seven companies, compared to the 13 in the original analysis, Dr. Carpenter, an expert witness of TransCanada, confirmed that these seven companies could still be relied upon as valid comparables for the Mainline.

Business risk

TransCanada indicated that the Mainline's supply risk, market risk, and regulatory risk would be unchanged under the proposed tolls compared to the risk that existed under the RH-003-2011 Decision. TransCanada indicated the application would reduce the Mainline's competitive risk, thereby reducing the fundamental business risk of the Mainline relative to the RH-003-2011 model. TransCanada submitted that competitive risk would decrease under the application for several reasons, including:

- The risk of bypass will be reduced;
- The contractual commitments provided by MAS under the Settlement will provide certainty of throughput in the future;
- The assignment of a large portion of the Bridging Contribution to Eastern Triangle reduces the risk that TransCanada would not be able to cover its investment on and of capital; and
- There will be reduced uncertainty over the future treatment of costs deferred in the TSA and LTAA.

Regarding variability risk, with the multi-year fixed toll, TransCanada indicated that under its application the Mainline will continue to be subject to earnings and cash flow variability on a year-to-year basis. TransCanada added it does not believe that the different (and symmetric) structure of the application's incentive sharing mechanism materially affects the Mainline's variability risk relative to the RH-003-2011 model. Dr. Carpenter reiterated that TransCanada is still under a fixed toll model as it was under RH-003-2011. In his view, there is no change to the fixed-toll aspect of that model; it changes other parameters but not variability risk.

In quantifying the change in business risk and its effect on the return, Dr. Carpenter added that the updated capital markets sample shows a reduction in capital market conditions and the cost of capital estimate of about 50 to 70 bps. Since the settlement ROE of 10.1 per cent on 40 per cent equity is about 140 bps lower than what the Board awarded TransCanada in RH-003-2011, that leaves roughly 70 to 90 bps that would be associated with the reduction of business risk under the Settlement relative to the decision model.

TransCanada submitted that the equity thickness of 40 per cent is unchanged from the RH-003-2011 Decision and therefore there is no alteration of the Mainline's financial risk in the application relative to the RH-003-2011 Decision.

Additionally, TransCanada submitted that Mainline tolls after 2020 could reflect a number of factors, including developments beyond cost-of-service regulation, that would address fundamental allocations of risk and reward between TransCanada and its shippers. TransCanada reiterated it remains committed to continuation of balanced and effective at-risk models for some or all of the Mainline's revenue requirement. TransCanada's witnesses were not averse to at-risk models in the future and accepted that TransCanada may have to work hard to get its revenue requirement.

Overall return on equity

TransCanada was of the view that the reduction of 140 bps from the 11.5 per cent ROE awarded in RH-003-2011 to the 10.1 per cent ROE in this application can be considered to fully capture both the reduction in competitive risk and the capital markets conditions as of the date of the Settlement.

Cost of debt

TransCanada confirmed it was seeking a return expressed on a by-component basis, which was the approach used by the Board in the RH-003-2011 Decision. TransCanada indicated it sought approval of its embedded cost of debt of the Mainline, which was comprised of both funded and unfunded debt. This debt cost was supported by schedules detailing the calculation of the Mainline's embedded cost of debt over the 2015 to 2020 period.

Views of Participants

ANE

ANE indicated the Board had insufficient evidence to make a determination on a fair return or of the appropriate debt equity ratio and that the balance of interests referred to in the Settlement is an insufficient basis upon which to set a return in accordance with the fair return standard.

ANE and Centra had further submissions regarding TransCanada's expected returns under the incentive mechanism. These submissions are discussed in section 7.2.

Centra

Centra agreed with TransCanada that the competitive and fundamental risk of the Mainline would be reduced if the application is approved, but differed on the extent to which these risks would be mitigated. Centra viewed this difference as being affected by TransCanada's proposal to retain unlimited pricing discretion under the application while retaining the ability to earn up to 11.5 per cent ROE with the incentive sharing mechanism.

Centra submitted that the application proposed to return TransCanada to cost-of-service recovery while maintaining unlimited pricing discretion and, by way of the incentive sharing mechanism, providing TransCanada with the opportunity to earn an ROE of up to 11.5 per cent. Centra's position was this directly contradicts the Board's RH-003-2011 Decision, which approved an ROE of 11.5 per cent for the Mainline in order to reflect TransCanada's increased level of business risk and because recourse rates were set at competitive levels (*i.e.*, below the levels at which TransCanada's revenue requirement would be recovered). Centra was of the view that the RH-003-2011 Decision deemed the Mainline to be much closer to a scenario wherein fundamental risk would have materialized if larger than forecast cost deferrals materialized.

Centra put forward its view that TransCanada's variability risk would be considerably less under the application for several reasons. First, absolute toll levels increasing relative to Compliance Tolls. Second, the ability to further adjust tolls for the 2018 to 2020 period after only three years. Third, the extent of market power associated with TransCanada's unlimited pricing discretion.

Centra was of the view that if the application was largely approved, including the proposed segmentation, a more appropriate approach to ROE would be to differentiate ROE by Mainline segment effective 1 January 2015, and for TransCanada to be subject to an earnings moratorium on the Prairies Line and NOL for the 2015 to 2020 timeframe, with these dollars being used to accelerate the depreciation of the Prairies Line.

TransCanada Reply

TransCanada rejected Centra's claim that variability risk is lower by stating that even with higher tolls, variability risk cannot be lower given that this risk results from the fact that tolls are fixed over the long term.

Regarding fundamental risk, TransCanada argued that the Mainline's business risk will remain relatively high under the application. TransCanada submitted that there is significant risk related to future cost recovery, particularly post-2020 on the Western Mainline, but also in the Eastern Triangle. A new toll design for the Western Mainline will not be implemented prior to 2020, at which time the remaining rate base of the Prairies Line will be approximately $1 billion. The NEB will set tolls that it determines are just and reasonable at that time. Thus, according to TransCanada, a considerable amount of uncertainty as to cost recovery of the Prairies Line rate base remains.

In addition, TransCanada submitted that while MAS members have committed in the Settlement to not bypass the Mainline through 2030, there is no such commitment by other shippers, and there is a risk that billing determinants will be reduced in the future should planned infrastructure in the northeastern United States materialize.

Mr. Reed submitted that while the Settlement reduces overall risk relative to retaining the model established by the RH-003-2011 Decision, it does not skew the risk/reward balance in favour of TransCanada or the shippers, nor does it reduce TransCanada's future risk of cost recovery post-2020 particularly on the Western Mainline.

7.1.1 Views of the Board

The fair return standard is used by the Board to guide decisions related to the allowed rate of return. A full fair return study allows the Board to evaluate whether the applied-for return would meet the criteria of the standard.[8]

In this case, TransCanada did not provide an extensive fair return study. However, the Board notes the unique circumstances surrounding this application, particularly the short time period between when the RH-003-2011 Decision was released and the commencement of the RH-001-2014 proceeding. The RH-003-2011 proceeding had an extensive examination of cost of capital issues, and the Board relied on fair return studies produced both by TransCanada and by CAPP. In that proceeding, the Board determined that the fair return on equity for the Mainline was 11.5 per cent on a 40 per cent deemed equity capital structure, after a full and comprehensive cost of capital examination was conducted.

[8] RH-003-2011 Page 147

By examining the changes in capital market conditions since the RH-003-2011 Decision, and changes in the Mainline's business risk under this application, evaluating the impact of those changes on fair return, and using informed judgment, the Board finds it has sufficient information to determine whether the application's proposed return is in accordance with the fair return standard.

The Board gave no weight in its determination to the submission that other pipelines have negotiated a return of 10.1 per cent, as the Board is of the view that negotiated returns are often not indicative as comparables when determining a fair return. Several aspects of individual settlements influence the agreed-upon return level, so it is inappropriate to assume that negotiated returns necessarily meet all the criteria of the fair return standard.

Capital markets

In this case, the Board gave significant weight to the evidence that indicated returns in the capital markets for a comparable pipeline sample (as determined in the RH-003-2011 Decision) have declined by 50-70 bps between the time the RH-003-2011 cost of capital evidence was filed and when the evidence for the current application was filed. This capital markets evidence was undisputed on the record. In the Board's view, it is imperative to take this updated capital markets information into account in determining a starting point from which the Mainline's changes in business risk can be assessed, and for the overall determination on fair return to be complete.

The Board finds that the capital markets would support a rate of return of 50-70 bps lower than the 11.5 per cent granted in RH-003-2011, before taking into account changes in the business risk of the Mainline.

Business risk

The Board agrees with TransCanada that business risk under the proposal will decrease materially relative to the RH-003-2011 Decision, primarily due to the Mainline's decrease in competitive risk under the application. This is influenced by the four reasons TransCanada provided, including the no bypass commercial commitment, and the commitments for some long-haul volumes to continue into the future. The ability of TransCanada to retain volumes on underutilized segments of the Mainline further reduces its business risk. These commitments are valuable to all shippers and reduce the overall risk of the Mainline.

In addition, the framework for collection of deferral accounts, including the LTAA and Bridging Contribution, significantly reduces the Mainline's business risk. All of the other elements of business risk, supply, market and regulatory risk, remain unchanged in the Board's view.

The Board finds that variability risk has not changed in an impactful way under the application. Given that tolls are proposed to be fixed for a multi-year period, variability in the Mainline's earnings and cash flows are not anticipated to be materially different under the terms of the application as compared to the variability risk under the RH-003-2011 Decision. The Board adds that there was no evidence submitted supporting that the Mainline's regulatory risk or financial risk would be altered by the application. The Board finds that these risks are unchanged under the application.

The overall result of these changes in risk is supportive of the applied-for decrease in return under the application.

Overall return on equity

As the capital markets evidence supported a reduction in return of the Mainline of 50-70 bps (before taking into account changes in risk of the Mainline under the application), the primary fair return determination the Board needed to make in this proceeding was whether the remaining decrease in the applied-for return – a decrease of 70-90 bps – was commensurate with the decrease in risk under the application. For the reasons discussed above regarding TransCanada's reduction in business risk, the Board believes that this decrease in return is reasonable.

Taking into account the decrease in business risk that the proposed tolls would facilitate, and the decrease in expected returns as supported by the capital market evidence on the record, the Board finds that the 10.1 per cent return on equity and 40 per cent deemed equity ratio is a fair return for the Mainline, commensurate with its risk under the proposal, and in accordance with the fair return standard.

Submission for separate returns for each segment and disallowance of return

While the Board sees merit in further examining the issue of segmented ROE in the future, the Board believes that the current integrated tolling methodology and integrated use of the system is supportive of a single system-wide ROE from 2015 to 2020. Further, the Board finds it is premature to disallow a return on any Mainline segment. The Board notes that in the context of the 2015 to 2020 period in the application, the Mainline is an integrated system that is transitioning toward a segmented system in the future. Therefore, the Board believes a single system-wide ROE of 10.1 per cent is appropriate, with no disallowance of return at this time. The Board finds that the Mainline is still in a position where it has a reasonable opportunity to earn a return on and of capital, and believes the proposed tolling methodology allows for this opportunity while maintaining just and reasonable tolls across the system.

The Board is ever mindful of its obligation to set just, reasonable, and not unjustly discriminatory tolls, and reiterates its finding, as indicated in the RH-003-2011 Decision, that there is a limit to the level of costs related to underutilization resulting from competition that Mainline shippers can absorb for tolls to remain just and reasonable. This limit has not been exceeded, and the proposal results in just and reasonable tolls.

The Board believes that with any specific proposal for a segmented toll methodology in the future, supporting analysis of the usage (expected and observed) of Mainline assets should be provided. If such an analysis does not support that the remaining Western Mainline assets in rate base are used and useful, then cost-of-service toll methodologies that necessitate recovery of all prudently incurred costs may not be appropriate. TransCanada has acknowledged this potential future circumstance, as indicated by its witness, Mr. Johansson, who submitted that TransCanada is prepared to employ at-risk models for the Western Mainline in the future.

Cost of debt

No parties opposed the proposed cost of debt for the Mainline, and no intervenors filed contrary evidence regarding the applied-for debt costs. The Board believes the proposed cost of debt is reasonable.

Decision

The Board finds that the 10.1 per cent return on equity and 40 per cent deemed equity ratio is a fair return for the Mainline, commensurate with its risk under the proposal, and in accordance with the fair return standard.

The Board approves the cost of debt as proposed by TransCanada and 60 per cent deemed debt ratio.

7.2 Incentive Mechanism

Views of TransCanada

The application includes an incentive sharing mechanism whereby net revenues would be calculated and shared based on a specific formula. TransCanada has stated that forecast net revenue for 2015 to 2020 based on the application's assumptions is zero, as the forecast revenue is equal to the forecast revenue requirement. If actual net revenue is positive in a given year, the benefit is to be shared between TransCanada and its shippers. Likewise if it is negative in a given year, that amount would be shared. The share accruing to shippers is made through an adjustment to the LTAA, with the share accruing to TransCanada retained as incentive earnings or losses.

In the application, net revenue is defined as a) forecast revenue requirement less actual revenue requirement plus b) actual revenue less forecast revenue. These forecast amounts were agreed upon by the settling parties. If net revenue is greater than zero, then TransCanada will receive 100 per cent of the surplus amount up to the amount required to offset TransCanada's after tax contribution ($20 million). The next $40 million of surplus net revenue is shared 25 per cent to TransCanada, and 75 per cent to shippers through the LTAA. Any additional surplus net revenue is shared with 10 per cent allocated to TransCanada and 90 per cent to shippers, again through a reduction to the LTAA.

If net revenue is less than zero, then 25 per cent of the first $40 million of deficiency in net revenue is to TransCanada's account, with the remaining 75 per cent accruing to shippers through an addition to the LTAA. Any additional net revenue deficiency is shared with 10 per cent accruing to TransCanada and 90 per cent accruing to shippers through an addition to the LTAA.[9] TransCanada proposed that the incentive sharing mechanism should remain in place for the period 1 January 2015 to 31 December 2020.

According to TransCanada, the Mainline's achieved ROE will be affected by the gains or losses arising from the incentive sharing mechanism, but cannot go below 8.7 per cent or exceed 11.5 per cent. The lower bound of 8.7 per cent is inclusive of TransCanada's $20 million after-tax contribution.

[9] There are some differences in the incentive sharing mechanisms in 2015, 2016 and 2017 as outlined in Section 7.3 of the Settlement application, due to stretch revenue assumptions as agreed upon in the Settlement.

Views of Participants

ANE

ANE submitted that the likelihood that net revenue deficiencies would materialize, or that TransCanada would not recoup its $20 million after tax annual contribution, appeared remote.

ANE indicated that since TransCanada was permitted to retain a portion of the net revenue benefits during the fixed toll period, the additional incentives equated to nearly $90 million and contributed to approximately a 300 bps increase in TransCanada's 2014 return above the 11.5 per cent return on equity approved by the Board in the RH-003-2011 Decision.

ANE submitted that the high tolls and low projection of billing determinants reflected in TransCanada's application virtually guarantee that it will over-recover Mainline costs, earn a rate of return of 11.5 per cent, and realize the benefits of substantial positive cash flows in each year.

ANE added that if the Board agrees with ANE that maintaining the tolling structure of the RH-003-2011 Decision is appropriate, and that a downward toll adjustment should be implemented to reflect the substantial TSA balance and increased throughput, then it would be appropriate for TransCanada to retain the ability to earn incentives through cost savings that have already been achieved.

ANE further suggested that if TransCanada continued to effectively withhold recourse capacity, then in addition to any additional directions that the Board deems appropriate, the net revenue incentive mechanism should be terminated and that TransCanada be placed at risk for any and all revenue losses attributable to bypass of its system.

Centra

Centra submitted that the application allows TransCanada to maintain the prospect of higher returns through unlimited pricing discretion and the incentive sharing mechanism while reverting to full cost of service recovery. The extension of unlimited pricing discretion to TransCanada would increase the likelihood of high revenues, and make achievement of an ROE well above the base case 10.1 per cent under the application quite realistic.

Centra's expert witness, Dr. Cicchetti, questioned the need for and purpose of incentive regulation for the Mainline, given his view that TransCanada had minimal risk in the 2015 to 2020 timeframe under the application.

TransCanada Reply

While Mr. Reed agreed that directionally TransCanada's business risk during the 2015 to 2020 period has been reduced, he indicated that through the incentive sharing mechanism, both its risk and potential benefit, have been balanced and bounded. This type of symmetric approach to risk and reward, according to Mr. Reed, is consistent with regulatory approaches taken by regulators for utilities throughout North America.

Mr. Reed also noted that while parties have made statements that TransCanada is virtually guaranteed to achieve an ROE at the top end of the range under the incentive sharing mechanism, they provide no support for such claim other than the experience to date since implementation of the RH-3-2011 Decision.

7.2.1 Views of the Board

While the Board finds that the Mainline's situation has improved since the RH-003-2011 Decision was rendered, it still faces significant challenges going forward, the most significant of which is underutilization on parts of the system. An incentive mechanism is a useful tool to help address these challenges. Primarily for this reason, the Board believes that an incentive mechanism is still an appropriate tool for the Mainline. Unlike the mechanism approved in the RH-003-2011 Decision, the proposed incentive sharing mechanism has both upside and downside risk for the Mainline on a year-to-year basis, and includes a contribution from TransCanada. The Board continues to believe that with a framework that provides the right tools to TransCanada and a properly structured balance of risks and rewards, TransCanada will have the appropriate means in place to continue to manage the issues facing the Mainline.

Centra's assertion that TransCanada has minimal risk under the proposal from 2015 to 2020 is not compelling. While the Board acknowledges the decrease in risk under the application, the Board is not persuaded that this justifies removing an incentive mechanism that will help TransCanada effectively manage its infrastructure, and has the potential to benefit shippers. Furthermore, the Board does not believe the application fully mitigates the Mainline's fundamental risk, particularly in the post-2020 timeframe. While the application decreases competitive risk, with a commensurate reduction in the return, the proposed incentive sharing mechanism also exposes TransCanada to some downside earnings risk on an annual basis with the potential to earn a lower return that did not exist under the RH-003-2011 Decision.

Regarding ANE's suggestion that if TransCanada withholds recourse capacity the incentive sharing mechanism should be terminated, the Board finds there is insufficient evidence on the record to make this determination.

The Board is fully cognizant of the fact that inherent in the incentive sharing mechanism proposal is TransCanada's ability to earn an ROE of up to 11.5 per cent. However, upon examination of the evidence, particularly exhibit B-25-1 which details the ROE levels that would be achieved based on net revenues, it is apparent that this level of return will not be achieved unless net revenues are in excess of $300 million dollars in 2015 and 2016, or approximately $300 million dollars in 2017. At net revenue levels such as these, the Board notes that the majority of the surplus will be credited to the LTAA. Further, any net revenues in excess of the amount required for TransCanada to earn a return of 11.5 per cent will be credited to the LTAA, net of tax effects. The Board believes this incentive mechanism will benefit not only TransCanada, but its shippers as well, without providing TransCanada upside potential rewards in excess of the level commensurate with its risk.

As noted in the discussion regarding the LTAA, section 5.2, the Board believes that the proposal to allocate the LTAA balance to the Eastern Triangle rate base in 2021 is reasonable at this point in time. However, should there be a material change in circumstances, this may no longer be appropriate.

Decision

The Board approves the applied-for incentive mechanism.

Chapter 8

2018 to 2020 Toll review

Views of TransCanada

To prevent materially different outcomes than expected over the 2015 to 2020 period, TransCanada proposed a review of tolls prior to 2018 for the 2018 to 2020 period. This review would include the forecast of annual revenue requirement and billing determinants for those years. Depending on the outcome of the review, TransCanada submitted that the tolls would be adjusted on a prospective basis and that TransCanada would also consult with Mainline stakeholders before any filing to the Board for approval of a toll change. TransCanada stated that it did not expect that other concepts, such as possible additions/removals from the LTAA, would be part of this review process, as the amortization of the LTAA will be based on the then current LTAA balance.

TransCanada noted that the settling parties determined that a review of forecast assumptions for the 2018 to 2020 period was appropriate as it denotes the mid-point of the six-year toll term and represents a reasonable period to evaluate the forecasting of annual revenue requirement and billing determinants to date. TransCanada further noted that, by 2018, the outcome of a number of planned infrastructure projects that could significantly affect the markets served off the Mainline should be known and may provide better information for forecasting billing determinants for the 2018 to 2020 period. This could result in adjustments to toll levels, but would provide toll stability for the remaining three years of the toll period.

Views of Participants

Ontario Ministry of Energy

Ontario argued that the Board should require that the review of tolls for 2018 to 2020 include consultation with all stakeholders and the inclusion of relevant information on all costs, billing determinants, the LTAA balance, the appropriateness of any remaining pricing discretion, and customer impacts as they relate to the proposed tolls for the 2018 to 2020 period. Ontario argued that the Board should remain engaged in obtaining information on customer impacts from TransCanada at regular intervals and from other stakeholders and then accelerate the review if warranted by the nature and extent of customer impacts.

TransCanada's Reply

TransCanada submitted that the Board should not consider conditions on the 2018 review from parties that have not submitted evidence in the proceeding.

8.1 Views of the Board

The Board expects tolls established for 2015 to 2020 to be substantially aligned with the underlying costs and revenues in each of those respective years. The Board notes that the compliance filing directed in Chapter 6 and the toll review for 2018 to 2020 will account for all changes to the revenue requirements and billing determinants, increasing the likelihood

that those tolls will more accurately reflect up-to-date revenue requirements and billing determinants. Further, all variances in cost-of-service items will be captured by the LTAA and the majority of any over or under recovery of revenue will go to the account of shippers.

The Board directs TransCanada to consult with all interested parties and to file an application prior to 31 December 2017 for approval of tolls for 2018 to 2020. The application must consist of:

- A review of revenue requirements, including return, income taxes, the ABA and the LTAA balance, for the 2018 to 2020 period;
- A review of billing determinants, including long-haul contracted quantities to the Eastern Triangle;
- A review of DMR forecasts for the 2018 to 2020 period; and
- A discussion of any other material changes that would impact the operation of the Mainline for the 2018 to 2020 period.

As discussed in Chapter 4, the Board approves the exercise of existing pricing discretion for the 2015 to 2020 period. However, the Board notes that the Mainline is moving towards segmentation and separate rate bases in a changing natural gas market. Once the term-up provisions are triggered or when new facilities are built, the Eastern Triangle segment of the Mainline will have a significant number of longer-term contracts and the segment will be highly utilized. On the Prairies and NOL segments however, underutilization is forecast to remain. The Board is of the view that the existing pricing discretion may not be required on all segments of the Mainline given that firm contract billing determinants in the Eastern Triangle may increase and contract durations may lengthen. In such a scenario, the need to use discretionary services to meet firm needs is unlikely to materialize and with it the need for the existing pricing discretion. For these reasons, the Board will review the continued appropriateness of the existing pricing discretion for the 2018 to 2020 period in the pre-2018 application.

The Board directs TransCanada to file the 2018 to 2020 toll application for approval regardless of whether it is expected to result in a material toll change. The Board has accepted TransCanada's forecast costs and revenues for toll-making purposes, subject to any updates included in the compliance filing. However, while the Board concludes that these forecasts are currently reasonable for toll-making purposes, the Mainline is in a transition period such that costs and revenues, including firm billing determinants and DMR forecasts, could deviate significantly from those included in this application. The Board agrees with TransCanada that the 2018 time interval ensures that all parties and the Board will have significantly more information on the impact on the Mainline of infrastructure projects. It also balances shippers' preferences for toll stability and predictability with the assurance that tolls will reasonably reflect the current circumstances of the Mainline.

Decision

The Board directs TransCanada to file an application prior to 31 December 2017 for approval of tolls for the 2018 to 2020 period.

Appendix I

List of Issues

The Board has identified but does not limit itself to the following issues for discussion in the proceeding:

1. Appropriateness of the proposed toll design for 2015-2020, including the consideration of the toll adjustment methodology, and allocation and treatment of the Long Term Adjustment Account and Toll Stabilization Account.

2. Appropriateness of the proposed revenue requirements and rate base over the 2015-2020 term including assumptions regarding costs, billing determinants and revenues.

3. Appropriate allocation of risks and rewards among TransCanada, Mainline shippers and other stakeholders over the 2015-2020 term, including return on equity and the proposed incentive sharing mechanism.

4. Appropriateness of continued pricing discretion for Interruptible Transportation and Short Term Firm Transportation services.

5. Appropriateness of TransCanada's proposed service modifications, including renewal provisions, contract terms, and conversion from long-haul to short-haul contracts.

6. Appropriateness of the proposed Bridging Contribution.

7. Appropriateness of the proposed framework for segmentation of the Mainline system post-2020, including information on cost allocation, asset values, and the future treatment of the Western Mainline under the proposed segmentation.

The Board will not consider toll levels and tolling methodologies related to specific *National Energy Board Act* Part III facility applications currently or anticipated to be before the Board. The Board will also not consider issues associated with abandonment funding, specifically regarding hearings MH-001-2012 and MH-001-2013.

Appendix II

Interim Toll Order

ORDER TGI-001-2014

IN THE MATTER OF THE *National Energy Board Act* (Act) and the regulations made thereunder;

AND IN THE MATTER OF THE an application filed with the National Energy Board (Board) by TransCanada PipeLines Limited (TransCanada) dated 20 December 2013 for approval of Mainline tolls effective 1 January 2015, pursuant to Part IV of the Act under file OF-Tolls-Group1-T211-2013-05 01.

BEFORE the Board on 18 December 2014.

WHEREAS on 10 June 2013 the Board issued Order TG-006-2013 approving final tolls for TransCanada for the years 2013 to 2017, effective 1 July 2013;

AND WHEREAS TransCanada filed an application dated 20 December 2013, seeking approval for a settlement under the *National Energy Board Guidelines for Negotiated Settlements for Traffic, Tolls and Tariffs* (Settlement Guidelines) including revised Mainline tolls to be effective 1 January 2015;

AND WHEREAS the Board ruled by letter dated 31 March 2014 that the application could not be approved as a contested settlement under the Settlement Guidelines; however the Board was prepared to consider it as a contested tolls application outside of the Settlement Guidelines;

AND WHEREAS TransCanada advised the Board by letter dated 14 April 2014 that the application should proceed as a common position of the parties to the settlement;

AND WHEREAS the Board issued Hearing Order RH-001-2014 dated 9 May 2014;

AND WHEREAS between 9 September and 25 September 2014, the Board held an oral public hearing in Calgary, Alberta during which time the Board heard evidence and argument presented by TransCanada and RH-001-2014 participants;

AND WHEREAS the Board's decisions on the application are set out in its Reasons for Decision dated December 2014, and in this order;

AND WHEREAS the Board has considered the evidence and submissions and has found that the tolls to be charged by TransCanada in accordance with this Order are just and reasonable and not unjustly discriminatory;

THEREFORE IT IS ORDERED, pursuant to subsection 19(2) and Part IV of the Act, that:

1. TransCanada shall cease to charge the tolls authorized in TG-006-2013 as of the end of the day on 31 December 2014.
2. TransCanada shall charge on an interim basis, the proposed tolls in the application effective 1 January 2015, pending any future amending Orders and/or final Order by the Board concerning Mainline tolls for 2015 to 2020.

NATIONAL ENERGY BOARD

Sheri Young
Secretary of the Board

Appendix III

Toll Order

ORDER TG-010-2014

IN THE MATTER OF THE *National Energy Board Act* (Act) and the regulations made thereunder;

AND IN THE MATTER OF THE an application filed with the National Energy Board (Board) by TransCanada PipeLines Limited (TransCanada) dated 20 December 2013 for approval of Mainline tolls effective 1 January 2015, pursuant to Part IV of the Act under file OF-Tolls-Group1-T211-2013-05 01;

BEFORE the Board on 18 December 2014.

WHEREAS TransCanada filed an application dated 20 December 2013, seeking approval for a settlement under the *National Energy Board Guidelines for Negotiated Settlements for Traffic, Tolls and Tariffs* (Settlement Guidelines) including revised Mainline tolls to be effective 1 January 2015;

AND WHEREAS the Board issued a letter dated 21 January 2014 soliciting comments from interested parties;

AND WHEREAS the Board received letters of comments with respect to the application from a number of interested parties by 7 February 2014 including TransCanada's reply comments;

AND WHEREAS the Board ruled by letter dated 31 March 2014 that the application could not be approved as a contested settlement under the Settlement Guidelines; however the Board was prepared to consider it as a contested tolls application outside of the Settlement Guidelines;

AND WHEREAS TransCanada advised the Board by letter dated 14 April 2014 that the application should proceed as a common position of the parties to the settlement;

AND WHEREAS the Board issued Hearing Order RH-001-2014 dated 9 May 2014;

AND WHEREAS between 9 September and 25 September 2014, the Board held an oral public hearing in Calgary, Alberta during which time the Board heard evidence and argument presented by TransCanada and RH-001-2014 participants;

AND WHEREAS the Board's decisions on the application are set out in its Reasons for Decision dated December 2014, and in this order;

THEREFORE IT IS ORDERED, pursuant to Part IV of the Act, that:

1. TransCanada must, for accounting, toll-making and tariff purposes, implement the directions and decisions outlined in the RH-001-2014 Reasons for Decision dated December 2014.

2. TransCanada must by 31 March 2015 prepare and file with the Board a Compliance Filing containing the following adjustments to the proposed tolls:

   - the actual TSA balance as of 31 December 2014 is to be allocated to the Long-Term Adjustment Account, following which the use of the TSA is to be discontinued; and,
   - all revenue requirements and firm billing determinants for 2015 to 2020 are to be updated as of 31 December 2014.

3. Interim tolls authorized in Order TGI-001-2014 will continue pending TransCanada's Compliance Filing and a final Order of the Board on Mainline tolls for 2015 to 2020.

4. The Long-Term Adjustment Account is approved as applied for during the 2015 to 2020 period.

5. The Bridging Amortization Account is approved as applied for.

6. Changes to existing services and new services are approved as applied for.

7. The term-up provision as applied for comes into effect on 30 March 2015.

8. An application for 2018 to 2020 tolls is to be filed for approval prior to 31 December 2017.

NATIONAL ENERGY BOARD

Sheri Young
Secretary of the Board

Appendix IV

Letter dated 31 March 2014

File OF-Tolls-Group1-T211-2013-05 01
31 March 2014

Mr. Bernard Pelletier
Manager, Tolls and Tariffs
Regulatory Services
TransCanada PipeLines Limited
450 First Street SW
Calgary, AB T2P 5H1
Facsimile 403-920-2347

Ms. Catharine Davis
Vice President
Pipelines Law
TransCanada PipeLines Limited
450 First Street SW
Calgary, AB T2P 5H1
Facsimile 403-920-2347

Mr. C. Kemm Yates, Q.C.
Blake, Cassels & Graydon LLP
3500 Bankers Hall East
855 Second Street SW
Calgary, AB T2P 4J8
Facsimile 403-663-2297

Dear Messieurs and Madame:

TransCanada PipeLines Limited (TransCanada)
Application for Approval of 2013 to 2030 Settlement Agreement (Settlement) Results of Comment Period

The National Energy Board (Board) has received TransCanada's application dated 20 December 2013, filed pursuant to Parts I and IV of the *National Energy Board Act*, the 2002 *National Energy Board Guidelines for Negotiated Settlements of Traffic, Tolls and Tariffs* (Settlement Guidelines) and the RH-003-2011 Decision. The application requests approval of a negotiated settlement respecting final tolls for services for 2015 to 2020 and for approval of a methodology for setting tolls to 2030.

TransCanada indicated that one factor that led to the filing of the application was the Board's expectation in RH-003-2011 that it file a tolls application in the event one of the "off-ramps" is reached before the end of the period of fixed tolls established in that decision.

On 21 January 2014, the Board issued a letter establishing a comment period on the Settlement application.

The Board received responses opposing the application, or parts thereof, by 3 February 2014 from: National Fuel Gas Distribution Corporation, Centra Gas Manitoba Inc., National Grid Gas Delivery Companies, Connecticut Natural Gas Corporation and Southern Connecticut Gas Company, Yankee Gas Services Company, Consolidated Edison Company of New York, New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation, Columbia Gas of Massachusetts, Canadian Association of Petroleum Producers, Northland Power Inc., BP Canada Group ULC and Alberta Northeast Gas, Limited.

In addition there were letters either supporting acceptance of the application, or elements of the application, or offering comments without taking a position received between 4 and 7 February 2014 from: Ontario Ministry of Energy, Statoil Natural Gas LLC, Industrial Gas Users Association, JP Morgan Commodities Canada Corporation, Association of Power Producers of Ontario (APPrO), Enterprise IFFCO Canada, ENN Canada Corporation, Tenaska Marketing Canada, Vermont Gas Systems, Inc., St. Lawrence Gas Company, Inc., Seneca Resources Corporation, Utilities Kingston, TransCanada Energy Ltd., BFI Canada Usine de Triage Lachenaie Ltée, Enbridge Gas Distribution Inc., Société en commandite Gaz Métro (Gaz Métro), Union Gas Limited, TransCanada, and Ministère des Ressources naturelles du Québec.

While the responses from Union Gas Limited, TransCanada, and Ministère des Ressources naturelles du Québec were received after the noon deadline, the Board has accepted each of these responses.

The comments received raised a number of areas of concern. They are:

1. The process used to arrive at the Settlement;

2. The form of the application; and

3. The process to be used to adjudicate the application, if required.

Process used to arrive at the Settlement

A number of submissions commented that the process used to arrive at this Settlement was not inclusive of all parties having an interest in TransCanada's traffic, tolls and tariffs. Further, several submissions raised the concern that the Settlement proposes fundamental changes to the tolling framework through 2030, including Mainline segmentation and cost allocation post-2020, without providing adequate detail or analysis of how they would work or what the impacts would be. These changes will change the gas transportation network in Canada but the Settlement was negotiated without the inclusion of parties like Northland Power Inc. and Centra Gas Manitoba Inc. who would be directly and substantially impacted by these changes.

The Board's Settlement Guidelines set out several criteria that should be satisfied in order for a settlement to be acceptable. The Board relies on an open and fair settlement process where a full range of interested parties are involved to result in a settlement that reflects the public interest. The Board uses the open settlement process to help in its assessment that the resulting agreement tolls are just and reasonable and not unjustly discriminatory.

Negotiated settlements are a give and take process where one party will give up something to gain something else. In assessing whether an applicant has justified the approval of a contested settlement, the Board will consider among other things, whether there is sufficient support for the settlement, based on the comments submitted by interested parties.

The settlement process must produce adequate information on the public record for the Board to understand the basis for the agreement, assess its reasonableness, and to be able to determine that the resulting tolls are just and reasonable and not unjustly discriminatory.

The form of the application

Some comments indicated that the application was filed as a negotiated settlement that did not meet the Board's Settlement Guidelines. Others indicated that it should be a review and

variance application, while others were of the opinion that it did not meet the intent of an "off-ramp" application under the Board's decision in RH-003-2011.

Views of the Board

The Board acknowledges that the Settlement is the result of significant work and negotiation by the parties. It is also a step forward in addressing capacity issues in the Eastern Ontario Triangle, a concern voiced in many of the comments received.

Process used to arrive at the Settlement

In this instance, the Board finds that the process used is insufficient to allow the Board to approve the Settlement as a contested settlement. The agreement negotiations included only TransCanada and its three biggest shippers, with other shippers being minimally involved after the agreement was nearly final. There are too many parties, including but not limited to Western Mainline receipt and delivery point shippers and those with differing Mainline utilization profiles, such as short haul shippers in the Eastern Ontario Triangle, who were not represented within the negotiation process of the agreement. The Board also finds that there are gaps in the adequacy of the record, such as information on the future treatment of the Western Mainline under the proposed segmentation, that arise at least in part from the under-inclusive process. For these reasons, the Board cannot determine that the resulting tolls are just and reasonable and not unjustly discriminatory.

The form of the application

The Board finds that the characterization of the form of the application is not as important as the content of the application. As such, the Board has before it an opposed application for approval of revised tolls.

Process to be used to adjudicate the application

The Board is prepared to consider this application as a contested tolls application outside of the Settlement Guidelines with the application being treated as a common position of the parties to the Settlement if so desired. TransCanada has until **14 April 2014** to advise the Board if the settling parties wish to proceed in this way, or if TransCanada plans to file an amended application. If TransCanada wishes to proceed, the Board will issue a hearing order in due course. If TransCanada does not wish to proceed, this matter is concluded.

TransCanada is directed to serve a copy of this letter on all parties to the Settlement, members of TransCanada's Tolls Task Force, all shippers on the TransCanada system, interested parties to NEB RH-003-2011, RH-001-2013 and RH-002-2013 proceedings and any other interested parties to the application.

Yours truly,

Sheri Young
Secretary of the Board